MULTIFAMILY ACCELERATED PROCESSING (MAP) Guide

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Office of the Assistant Secretary for Housing–FHA Commissioner

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Section	Highlights
	Chapter 1 - Introduction
Section 1.3	Added Sections 231 Housing for the Elderly as a new program eligible for processing under MAP. Section 232, Residential Care Facilities, was deleted from the MAP Guide because it is no longer eligible for processing under MAP/TAP. The program has been transferred to the Office of Insured Health Care
1.3.C.3	Reference to New Project Concept Meetings stage.
1.3.C.2A	One half of the application fee is due with the submission of market rate Pre-applications and the entire application fee due at the Firm Commitment stage for "affordable" new construction, substantial rehabilitation, and Section 223(f) applications.
1.4D	Clarifies waiving of the MAP Guide Sections.
	Chapter 2 - Lender Qualifications
2.1	Was modified to clarify underwriter and third party approval procedures by the HUBs/Program Centers. The revised section reinforces existing guidance on the procedures for approving underwriters and third party contractors, and the procedures to be followed for third party contractors and underwriters that have unsatisfactory performance histories.
2.2	Was corrected to reflect existing practice of MAP Lenders approval by the Director of the Office of Multifamily Housing Development, as opposed to the Deputy Assistant Secretary (DAS) of Multifamily Housing.
2.3	Was modified to reflect new guidance regarding MAP training. MAP training will now be offered quarterly by HUD Headquarters at various locations throughout the country.
2.3 & 2.8	Was modified to reflect revised new worth and liquidity requirements in accordance with 24CFR Part 202.6 and 202.7, published April 1, 2010
2.4	MAP Lender In-house Underwriter Approval Requirements
2.6	Identity of Interest between Map Lender and Tax Credit Syndicator.
2.10 - 2.15	Deleted/Moved to new Chapter 15.

Chapter 3 - Eligible Multifamily Mortgage Insurance Programs

	General – All Housing Notice 2010-11, Risk Mitigation (RM) Loan Ratios and Debt Service Coverage Ratios are detailed under the respective program areas.
	The removal of Section 232 Residential Care Facilities as an eligible MAP program.
3.2	Discusses new RM application fee payment requirements for proposal types; eliminates inspection fee for zero repairs and sets new threshold; conditionally accept 2530 minor issues; covers RM initial operating deficit; defines RM Affordable Housing; announces furnished units/corporate leases; new RM replacement for reserves requirements; RM new Condo regimes.
3.2.B	Single Asset Entity Requirements.
3.2F	Application fee modification
3.2.G	Section 207/223(f) inspection fee requirements expanded.
3.2.J	Correction of Fair Housing Act Violations.
3.2 K	Previous Participation Electronic System (APPS).
3.2.P	Operating Deficit has new parameters when residents are displaced.
3.2.Q	Definition of affordable housing.
3.6	Section 221d3 explains requirement to reserve credit subsidy and explains maximum loan ratios and debt coverage ratios implemented by the RM Notice.
3.7	Section 220 new RM relationship between LRs/DSCRs and commercial space and separate commercial analysis requirement.
3.8.A	Introduces Section 231 Housing for the Elderly as an eligible MAP program & eligible for review by the National Loan Committee.
3.9	Treat a Section 223(f) application with both a purchase and a refinance transaction, as two separate transactions.
3.9.R	Section 223(f) introduces the new equity out require to hold half of the equity for release until all repairs are complete.
3.9.Q	Section 223(f) occupancy standards underwriting guidance explained.
3.9.R	Section 223(f) consideration of obtaining a market study explained.

Chapter 4 - Application Requirements

4.1 B	Two stage processing or opting to combine both into the Firm Commitment stage.
4.2.A	New Project Concept Meeting.
4.2.A.1.c	Pre-Application stage requires preliminary appraisal work & the Lender's creditworthiness assessment of the sponsor & $250M HUD pre-approval.

4.2.C	New pre-application fee requirement.
4.2.D.3	Authorize three 30-day extensions or one 90-day extension.
4.3.C	Submission of a completion application is one original and one electronic copy.

Chapter 5 - Architectural Analysis

5.1.A.1	Qualifications of Lender's Needs Assessor.
5.1.C	HUD approval of Lender's Needs Assessor.
5.2.A	Expanded to include new Architect's Professional Liability Insurance.
5.4	Adds instructions to prepare or review the reserve-for-replacement analysis where the formula has been waived. Refers to 5.28 for LIHTC streamlined processing.
5.6	Adds preparation or review of the reserve-for-replacement analysis where the formula has been waived to the architectural analysts report.
5.5.B.3	Acceptability of an existing survey market "re-surveyed."
5.7.C.3.d	Lender's authorized signatory is the only one who can sign the plans and specifications for the Lender. Lender must supply HUD with the name(s) of the authorized signatory.
5.8, 5.15, 5.21, 5.22, 5.24	Refers to 5.28 for LIHTC streamlined processing
5.17	Added provisions regarding the hiring of a qualified LBP and/or asbestos abatement contract if a project is determined to have either of these conditions.
5.9	Adds HUD review of the reserve-for-replacement analysis where the formula has been waived. Refers to 5.28 for LIHTC streamlined processing.
5.24.B	Properties dating from the 1970s which contain hazardous aluminum wiring must undertake mitigation measures as a condition of Section 223(f) mortgage insurance.
5.24.C	Smoke detectors are required in Section 223(f) projects.
5.24	Expands instructions on the Fair Housing Act Accessibility considerations on structural modifications/retrofits for Section 223(f) projects.
5.25.C	For a project with more than one structure, the Lender must prepare a Dwelling Unit Breakdown list and an estimate of the Gross Floor Area for each individual structure in the project.
5.26.A.2	Updating of PCNA when 120-day period expires.
5.26.D.2.d(3)	Added that the construction contract contains latent defects assurance language.
5.28	LIHTC streamlined processing instructions has been added.

Chapter 6 - Cost Processing

6.1	Allows the underwriter to serve as the cost analyst if technically qualified.
6.2	Section 231 was added. Adds the requirement to estimate the costs for reserve-for-replacement deposit where the formula has been waived and to submit with the firm package.
6.2, 6.4, 6.5, 6.6, 6.7, 6.8	Refers to 5.28 for LIHTC streamlined processing.
6.3.C.3.b.(1)	Section modified to eliminate Site Not Attributable.
6.3.C.3.d (3)	Ceiling for Rehabilitation Cost Not Attributable.
6.3.C.3.f	Eliminated the entire Section on Site Not Attributable
6.9.B.2	Independent Lender review of repair costs in PCNA is a required Firm stage deliverable.
6.9.2.A.1	PCNA prepared by Lender's Needs Assessor.
6.10.1	Lender Project Processing – Firm Stage
6.10.2	HUD Procedures

Chapter 7 - Valuation Processing

7.3.A.6	If the subject property contains commercial space, the appraiser must have experience in the appraisal of commercial properties.
7.3.C.4	If the subject property contains commercial space, the analyst must have experience in the completing market studies on commercial properties.
7.4.A	Appraisal and Market Study should be completed by separate entities.
7.4.B.3	Market Study Effective Date. For pre-applications, the effective date of the study must be within 120 days before the date the pre-application package is submitted.
7.4.B.8	The market analyst may not consider, analyze, or report any information that makes reference to race, color, sex, handicap, familial status, religion, or national origin of the geographic area, neighborhood, occupants, owners or prospective owners.
7.5	Guide for Content and Format of a Market Study for General Occupancy Rental Housing – Was formerly in the appendix.
7.6.A.1	The appraisal must identify the United States Department of Housing and Urban Development as an authorized user of the report.
7.6.A.3	Instructions for complex or unusual appraisal assignments.
7.6.A.6	The USPAP Jurisdictional Exception rule is not generally applicable. New Occupancy Percentages

7.6.A.9	Substantial rehabilitation cases under Section 231 differ from Sections 220, 221(d)(3) and 221(d)(4) cases in that a market value based on the completion of the rehabilitation is required.
7.6.A.10	New and extensive instructions relating to Remaining Economic Life (REL).
7.6.A.15	New Inspection Requirements.
7.6.A.16	Appraisal Exhibits.
7.6.A.17	New Market Analysis Requirements.
7.6.B	USPAP certification must include statement that racial/ethnic composition in no way affected the appraisal determination.
7.7.G.1	Provide data to support the subject's commercial vacancy rate in relation to the market commercial vacancy rate and review the rollover risk and cost of resident improvements to re-lease space.
7.7.M	Other Income- More extensive guidance on ancillary and commercial income, short-term lease premiums, corporate leases and ineligible income.
7.8.C.3	Reserve for Replacements. New instructions. This was previously in its own section.
7.9.B.3	Instructions on Site Analysis with respect to crime rate.
7.9.I	Site Value for Subsidized and/or Low Income Housing Tax Credit Applications – New Instructions.
7.9.J	Excess Land. Warehousing of "excess" land area is not encouraged but where un-avoidable, it may be permitted without the advance of insured funds.
7.10.A.9	Estimate of the warranted price of the land or "as is" value for substantial rehabilitation cases is now required at Pre-Application.
7.12.A.6	Environmental Assessments are required for all 223(f) (including 202/223(f)).
7.12.B.1	Conflicts between Appraisal and Underwriting. The Lender must state any reasons for disagreement with the appraisal report.
7.13.F	New Instructions for Contingency Reserves. This percent may range between 10 percent and 15 percent.
7.13.G	Interest During Construction. New Instructions.
7.14.A.3	Initial Operating Deficit. Absorption period and rate are defined. Due to volatility and weakness in the real estate markets.
7.16.A	Tax Abatement Procedures. There are now three exceptions. This was formerly the section for Site Not Attributable (SNA). The term SNA has been eliminated.
7.16.C	Value/Mortgage Proceeds associated with Short Term Abatement.
7.17	New Chapter on Section 8 and LIHTC Processing.

Section	***Chapter 8 - Mortgage Credit Underwriting and Processing Requirements***
	Risk mitigation underwriting changes to debt service coverage, loan to value, strengthened credit and financial analysis, i.e. key principals must meet a threshold of $250,000 before submitting an application.
8.2.A	Pre-application requirements and guidance expanded.
8.3.A.5	Emphasize credit & financial analysis of key principals including fully funding borrower entity.
8.3.B.5	Fannie Mae form will replace request for verification of deposit.
8.3.C.1	Identifying the Borrower and Its Principals expanded.
8.3.D	Paragraph *Identifying The Principals*, revised to add LLC managing members, passive investors.
8.3.I	"Rejection Because of Unacceptable Credit", bankruptcy, insolvency, pending litigation with HUD and the REO schedule.
8.3.K	Concentration on principal's risks that meet the threshold of $250,000.
8.4.B.2	The requirement for submission of three year balance sheet is expanded.
8.4.A.5	Real Estate Owned Schedule & Mortgage Debt Schedule discussed.
8.4.B.2.d	Added "Schedule of Real Estate Owned" & "Schedule of Mortgage Debt".
8.4.B.3.a	Increased requirements for Section 223(f) financial analysis.
8.4.B.3.d	Past due accounts payable and project liabilities must be cleared and released, or otherwise fully satisfied before closing.
8.4.C	Expanded the requirements of financial statement analysis.
8.4.C.2	Fully funded borrower entity is required to submit financial statements.
8.4.C.14	Add Historic & New Market Tax Credit transactions and expanded to address LIHTC syndicators.
8.8.A.1.c	This paragraph was modified to remove Site Not Attributable (SNA) & replace with the warranted price of land.
8.8.A.2.d	Fifty percent of cash out from mortgage proceeds will be held in escrow until non-critical repairs are complete.
8.8.C.4	Provides guidance on mezzanine debt.
8.8.C.5.a	Recent indebtedness defined.
8.9.B.1, B.2	New guidance for Secondary Financing from Government Sources and Private Sources.

8.9.B.1	Added procedures for handling mezzanine financing.
8.9.E.	Tax credit equity syndicators or investors (with or without an IOI may make equity bridge loans on tax credit projects.
8.10.A	Added to update firm commitment process instructions to consider the use of syndication proceeds.
8.10.B	New guidance on non-disclosure of grants and loans.
8.11	Subsidy layering review eliminated on Title II mortgage loans.
8.11.A	Introduction paragraph on evaluation on nonprofit mortgage/sponsor expanded.
8.11.A.9 new	Added the requirement for written explanation of non-performing assets.
8.11.B	Added a property manager and asset manager resume requirement when applicable.
8.11.B	Added no material, unmitigated contingent liabilities to the financial statement analysis.
8.11.B	Added requirement to determine if the nonprofit has a proven record of raising sufficient funds to meet its operating needs.
8.11.C.1.e	Added must not have any unresolved internal control or compliance findings; unresolved issues of integrity or conflict of interest.
8.11.C.2.a	Added residential credit reports.
8.12	Added working capital and operating deficit requirement to Insurance Upon Completion transactions.
8.13.E	The working capital escrow percentage increased from 2 to 4 percent.
8.13.F	The operating deficit escrow is now based on the greater of the appraisal & underwriting analysis, 3 percent of mortgage amount or 4 months of debt service.
8.13.J	Cash out for land equity and other equity is deferred until final endorsement.
8.13.K	Addresses the HERA 2008 and 24 CFR 200.54 provision of the tax credit equity contribution required at initial endorsement.
8.14.C.5	Excess premium income on Section 223(f) applications.
8.14.B	Removed variable rate policy as it is not permitted.

Chapter 9 – Environmental

9.2.B	Now, the FECO must also be given the opportunity to review and comment on any environmental assessment in which the project is in the normally unacceptable or the unacceptable noise zone. This is regardless of the size of the project.
9.2.A.1	Lead-based Paint (LBP) Chips. This section clarifies that LBP chips that are not inside or part of a structure may be deemed to be a hazardous substance under

	CERCLA.
9.3	Expanded to include the requirements that the environmental professional firm conducting the Phase I must base is site analysis on the guidelines in the listed publications of the American Society of Testing materials (ASTM).
9.3.C	Discussion of remediation plans.
9.3.E	States that HUD will not accept property for firm commitment where a site contamination problem has been capped or paved over.
9.3.F	Discussion on Monitoring wells.
9.4	Details on field personnel responsibilities in reviewing cases requiring remediation; and remediation cost included in the mortgage.
	The following subsections in Section 9.5, "Environmental Report" contain more detailed clarifications:
9.5.A	Lead Based Paint
9.5.B	Asbestos
9.5.C.2	Historic Preservation
9.5.D.2	Floodplain Management
9.5.I	Coastal Zone Management

Chapter 10 - Management Analysis

10.2.A.1	Added option to file electronic HUD-2530 through – Active Partner Performance System (APPS) Participant Certification page.
10.2.A.7	Exhibit requirement added for marketing, leasing and relocation plan.
10.4	HUD Review of the Previous participation Certification (Form HUD-2530) - Active Partners Performance System (APPS).
10.9	New Section discusses Asset Management approval to release an operating deficit escrow.

Chapter 11 - Lender Underwriting - HUD Review

11.1.B	Added the risk mitigation pre-application fee structure.
11.1.C	Added in a signature requirement for the Underwriter's Narrative Summary.
11.1.D	Added the risk mitigation on-site lease audit and physical inspection requirement.
11.2.G	Basis for additional FO review.

11.2.G Note	Discusses extension of time for reviews.
11.2.H	Expanded the HUD review recommendation memorandum instructions
11.2.I.2 & 11.2 L.8	Added early start construction to the firm commitment decision Section & these requirements cannot be waived.
11.2.L.7	Paragraph modified to remove Site Not Attributable.

Chapter 12 - Construction Period

12.6.A.4	HUD Construction Contract takes precedence over inconsistent provisions in AIA Document A201, General Provisions, Article 9.8.
12.8.A.5	Working capital construction contingency.
12.15.C.3	Updated the release of working capital.
12.15.D	Explains risk mitigation contractor 10% retainage and discusses reducing the retainage beyond 50 percent completion until 100 percent complete.
12.15.E	Provides the risk mitigation release procedures for the initial operating deficit escrow.
12.15.F	Provides the risk mitigation cash-out from land equity guidance.
12.16.M	Added the working capital and operating deficit requirement for IUC applications.
12.17.A.3	Adds risk mitigation guidance on the release of fifty percent cash out escrow when the non-critical repairs are complete. New modified escrow Form HUD-92476.1M

Chapter 13 - Cost Certification

13.2 & 13.5	Eliminated need for cost certification on LIHTC, Historic tax credits, or New Markets tax credits projects where the ratio of the loan proceeds to the actual cost of the project is less than 80 percent.
13.4	Projects Exempt from Cost Certification, because of HERA 2008.
13.7	Was revised to define substantial completion and final completion.
13.11.B.4.c	Non-disclosure of liabilities on balance sheets.
13.11.C.5	Added Form HUD-2205-A.
13.15.H.3.b. NOTE	Included the permanent Lender's fee up to 5-1/2 percent for bond-financed projects.
13.24	New section on authorized reopening of mortgage transaction when a mortgage is increased.

13.25	New section on Deferment of Principal Payments was added.
New Chapter	***Chapter 14 – Low Income Housing Tax Credit (LIHTC) Guidance***
	Chapter 15 - Quality Assurance Enforcement Actions
15.2B	Removed recommendation of MAP Lender Review Board for Program Center Directors.
15.2.B, C & D	Clarified existing policy that warning letters shall be referred to the Lender Qualification and Monitoring Division.
15.4	Replaced the referral to the MAP Lender Review Board to the Director of MF Development.
15.8.E	Removed references to Chapter 2, added language for clarity.
15.9.B.6	Clarified the duration or provisions modified in settlement agreements.
15.9.C	Clarified that the MAP Lender's compliance is determined by HUD.
15.15	Removed the term "informal" from this section.
15.15.D	Clarified duration of time before the Appeals Official makes a written determination.
New Chapter	***Chapter 16 - Master Lease to facilitate the use of tax credits***
New Chapter	***Chapter 17 - Refinancing Cooperative Housing Projects under Section 207/223(f)***

Chapter 1

Introduction

1.1 MAP and the Guide

Multifamily Accelerated Processing (MAP) is designed to establish national standards for approved Lenders to prepare, process and submit loan applications for Federal Housing Administration (FHA) multifamily mortgage insurance. The MAP Guide provides - in one volume with appendices - mortgage insurance program descriptions, borrower and Lender eligibility requirements, application requirements, underwriting standards for all technical disciplines and construction loan administration requirements.

Statutory authority for the implementation of MAP is contained in the basic insuring authority for each of the programs covered in MAP, pursuant to the National Housing Act, Sections 220, 221(d)(3), 221(d)(4), 231, 223(a)(7) and 223(f). Additionally, Section 211 of the National Housing Act authorizes the Secretary to make such rules and regulations as may be necessary to carry out the provisions of the Act. The FHA requirements listed in HUD regulations covering each MAP eligible program are fully described in this MAP Guide.

1.2 Purposes of MAP

The MAP program is intended to provide a consistent, expedited mortgage insurance application process at each HUD Multifamily Hub or Program Center (PC). HUD no longer accepts new applications for the covered programs, either for pre-application review or for Firm Commitment review, under local "fast-track" processing. Additionally, all MAP eligible projects must be submitted using MAP processing and may no longer be submitted under Traditional Application Processing (TAP). FHA approved multifamily Lenders who are not approved to submit MAP applications can submit loans for mortgage insurance using TAP.

Some MAP-approved Lenders only originate loans and do not service them. After obtaining a Firm Commitment for mortgage insurance under MAP, the originating Lender may sell or transfer the Firm Commitment to another MAP Lender. The second MAP Lender will close the loan, oversee the construction loan administration, if applicable, and service the loan in accordance with HUD requirements. At the pre-application submission, the originating Lender should inform the Hub/PC if it does not intend to service the loan or administer the construction loan, and identify which Lender will be responsible for those functions. The second Lender must identify their construction loan administrator before or at initial endorsement. A loan servicer who receives a transferred MAP loan for servicing must be FHA-approved for multifamily housing, but it need not be a MAP-approved Lender for originations.

MAP is intended to:

A. Establish a process that significantly reduces the amount of HUD review time.

B. Strike a careful balance between expedited processing and ensuring an acceptable level of risk management for HUD's multifamily mortgage insurance programs.

C. Have in one volume, the MAP Guide, the basic information required for loan origination by the Lender and for review by HUD staff.

D. Bring Handbook and Notice instructions current and maintain up-to-date instructions through amendments to the MAP Guide.

E. Provide the Lender with predictable and consistent underwriting guidelines, thus facilitating efficient processing and better service for borrowers.

1.3 Brief Summary of MAP

A. Lender Qualifications and Monitoring

By permitting a MAP Lender to prepare much of the documentation for a loan submission for mortgage insurance, HUD places confidence in the Lender's integrity and competence. Lenders wishing to submit MAP applications for mortgage insurance must be:

1. An FHA approved Lender. See the Mortgagee Approval Handbook (4060.1).
2. Approved by the Lender Qualification and Monitoring Division (LQMD) in HUD Headquarters' Office of Multifamily Development. See Chapter 2 of the MAP Guide.
3. Subject to Quality Assurance Enforcement Actions. See Chapter 15 of the MAP Guide.

B. Programs Covered by MAP

MAP may be used for Sections 221(d) (3) and 221(d) (4) (new construction or substantial rehabilitation of apartments), Section 220 (new construction or substantial rehabilitation of mixed use projects in urban renewal areas), Section 223(a)(7) and Section 223(f) (refinancing or purchase of existing apartments), Section 231 Housing for the Elderly, and Section 241(a) Supplemental Loan program. HUD will publish additional program guidance for Sections 223(a)(7) and 241(a) in a future release.

C. Processing

1. For market rate new construction or substantial rehabilitation proposals under Sections 220, 221(d)(3), (d)(4), 231, and 241(a), there is a two-stage application review process: Pre-application review and an application for Firm Commitment review. For refinancing or purchase under Section 223(f) or 223(a) (7), the Lender must only file an application for Firm Commitment. Before most applications are filed, the Lender will request and attend (in person or by conference call) a concept meeting with the Hub/PC to discuss the proposal. After the concept meeting, applicants for affordable new construction or substantial rehabilitation may combine the pre-application and Firm Commitment stages and submit a single application directly for Firm Commitment.

2. HUD requires a fee of $3 per thousand dollars of the requested mortgage amount for review of the Firm Commitment application. For market rate transactions, one half of this amount, which is non-refundable, is due with the submission of the pre-application package and the other half is due with the application for Firm Commitment. For affordable new construction or substantial rehabilitation proposals and for any refinancing or acquisition transactions, the entire amount is paid at the Firm Commitment stage.

3. The following is the process for a Lender to submit either a pre-application or application for Firm Commitment.
   a. The Lender must have a "concept" meeting with the Hub/PC to discuss the proposed transaction if it involves new construction/substantial rehabilitation or a refinance or acquisition transaction which has any significant issues, has cash out or is a large loan. The exhibits submitted for a concept meeting are in Appendix 4A (new construction/ substantial rehabilitation) and Appendix 4B (refinance or acquisition).
   b. If the Hub/PC approves the application submission after the concept meeting, the transaction will be entered into the Development Application Processing (DAP) Tracking subsystem where it will be assigned a Project/FHA Number. The Lender will select and is responsible for the third party due diligence team and must request approval of the MAP underwriter. If there are concerns about the third parties or the proposed underwriter, the Hub/PC will advise the Lender and contact LQMD, if appropriate.
   c. The Lender will collect data, processes the loan, perform due diligence, underwrite the loan, obtain internal loan approval (from the Lender's loan committee or other process), and submit the loan application and fee to the appropriate Hub/PC.
   d. The Hub/PC staff will review the application to determine that it is complete and there are no material deficiencies or obvious issues not addressed in the application. If the Hub/PC determines that the application is complete and ready for processing it will accept the application fee and continue the technical review. If there are material deficiencies identified, they will be discussed with the Lender and documented in an e-mail or by letter. If the issues are corrected within 5 business days, processing may resume. If the issues cannot be corrected within the 5 business days or at such other time frame as the Hub Director determines as appropriate, the application will be returned to the Lender.

4. Standard Processing Times

   NOTE: The processing times listed in this section are under review and are subject to change by HUD in a future release.

   The time frames for processing listed below have been established to assure timely decision making on MAP applications. These processing time frames are in business days, not calendar days.

   a. Pre-application Review (New Construction/Substantial Rehabilitation) – 45 days.

      Measured from when HUD receives a **complete** pre-application and ending when HUD issues an invitation letter that advises the Lender to apply for a Firm Commitment.

b. Firm Commitment Application Review (New Construction/Substantial Rehabilitation) - 45 days.

Measured from when HUD receives a complete Firm Commitment application and ending when HUD issues a signed Firm Commitment letter. The MAP Team Leader may extend this review period under certain circumstances as described in Chapter 11, Section 11.2. Lenders will be advised if the Team Leader determines that a more extensive review is needed.

c. Firm Commitment Application Review (Existing Property Purchase or Refinance) – 60 days.

Measured from when HUD receives a complete Firm Commitment application and ending when HUD issues a signed Firm Commitment letter.

d. Combined Pre-application & Firm Commitment application - 60 days.

For where the Lender has submitted a combined Pre-application and Firm Commitment application for an affordable transaction, measured from when HUD receives a complete application with all of the exhibits required for Firm Commitment processing.

5. HUD has certain responsibilities which it does not assign to the Lender, including responsibility for the environmental clearance on Form HUD-4128 (even though the Lender prepares information for HUD's review), approval of the owner's Affirmative Fair Housing Marketing program, and issuing the commitment for mortgage insurance.

D. Construction Responsibilities

1. Under MAP, HUD must approve the initial and final draws.
2. HUD will perform inspection duties and will provide copies of the Trip Report to the MAP Lender.
3. The MAP Lender will prepare and approve the documents required for the interim draws during construction.
4. HUD must approve the construction amount for each item in the initial and final advance, and for each Change Order during construction.

E. No New Requirements for Servicing

MAP makes no changes in procedures for servicing or asset management. See Section 1.2 above for guidance on MAP-approved Lenders who only originate loans and transfers the loan to another FHA-approved Lender for servicing.

1.4 Relation of MAP to Handbooks, Notices and Regulations

A. All applicable HUD Handbooks, Notices and Forms remain in effect and will be used for traditional HUD processing of mortgage loan applications. For applications under MAP, the Guide incorporates the majority of Handbook, Notice and Form requirements and includes in the Appendix the forms that are required for most applications. Certain forms and requirements that are infrequently used or are too detailed for inclusion in the Guide are referenced. If there is a conflict between the Guide and the Handbooks, the Guide will take precedence. Lenders with questions should address them to the Hub/PC processing the application. Where the Guide is silent on a matter, the Lender should consult with the Hub/PC through the following MAP website: **http://www.hud.gov/offices/hsg/mfh/map/maphome.cfm.**

B. Consistent with their level of approval, the Lender must be familiar with the basic programmatic requirements and regulations of the insurance programs set forth in 24 Code of Federal Regulations Part 200.

C. The Lender is encouraged to contact a Hub/PC if any issues are not addressed in the Guide or if any clarifications are needed. See Chapter 11 on Underwriting for waiver procedures. The Hub Director may waive non-regulatory or non-statutory provisions of the Guide, although Chapter 11 specifies a number of requirements that may not be waived without prior approval of HUD Headquarters (HQ). Regulatory provisions may be waived only on approval of the Assistant Secretary for Housing - FHA Commissioner. Statutory provisions may not be waived.

D. Any waiver of this Guide granted by the Hub Director must be documented in the Hub/PC docket and the Washington docket, along with the Lender's request and supporting documentation for the approval. Waivers must be submitted, to the HUD HQ Office of Multifamily Housing Development, Attention: Technical Support Division for tracking and post review. HQ will review all waivers granted to determine if changes to the Guide or to the regulations are appropriate.

E. Program Obligations. HUD recently made technical and substantive changes when it adopted new and updated FHA multifamily loan closing documents. The term "directives" has been eliminated and substituted with the term "Program Obligations." "Program Obligations" means:

1. All applicable statutes and any regulations issued by the Secretary pursuant thereto that apply to the Project, including all amendments to such statutes and regulations, as they become effective, except that changes subject to notice and comment rulemaking shall become effective only upon completion of the rulemaking process, and
2. All current requirements in HUD handbooks and guides, notices, and mortgagee letters that apply to the Project, and all future updates, changes and amendments thereto, as they become effective, except that changes subject to notice and comment rulemaking shall become effective only upon completion of the rulemaking process, and provided that such future updates, changes and amendments shall be applicable to the Project only to the extent that they interpret, clarify and implement terms in the relevant document name rather than add or delete provisions from such document. Handbooks, guides, notices, and mortgagee letters are available on HUD's official website: (http://www.hud.gov/offices/adm/hudclips/index.cfm or a successor location to that site).

1.5 Work Management

A. Applications for mortgage insurance should be submitted to the MAP Coordinator in the Hub/PC having jurisdiction for the area where the property is located. The Hub/PC Director is responsible for workload management within their Hub/PC, including:

1. Delegation and staff assignments,
2. Priority of application processing,
3. Meeting standard processing times, and
4. Loan Committee.

B. Responsibilities assigned by the Guide to a Hub/PC Director may be delegated unless specifically restricted by the Guide, statute or regulation or by existing published delegations of authority.

C. Washington Docket. At the "initial"/ "final" endorsement and closing, the Hub Director should assemble a set of original documents (or as HUD allows, copies) for the Washington Docket, in accordance with the requirements and procedures set forth in the MAP Guide Appendix 11E. If originals of recorded documents are unavailable because of filing or recording procedures, a completely legible copy should be collected (certified true and correct by the recorder or by the title company). Note that the Phase I Environmental Clearance is a program requirement and a supporting document for form HUD-4128, *Environmental Assessment and Compliance Findings for the Related Laws*. It should remain with the HUD-4128 in the Washington Docket as a part of the permanent, historical file.

D. Initial Endorsement Diligence Review. In connection with initial endorsement and closing, the Hub Director and program staff will review the materials submitted in accordance with Program Obligations. In this review, the Hub Director and program staff should confirm the information listed on the Initial Endorsement Diligence Review Worksheets, attached in the MAP Guide Appendices 11A – 11D, and may utilize such worksheets to document compliance with Program Obligations.

NOTE: It is expected that the content contained in this chapter will be replaced by a new Regulation adopted by the Department to implement and govern a MAP Lender and Underwriter qualification system, which is expected to be adopted later this calendar year after public notice and comment.

Chapter 2

Lender and Underwriter Qualifications

2.1 Introduction

A. MAP requires Lenders and Underwriters to be skilled in underwriting multifamily housing loans and in preparing applications for FHA multifamily mortgage insurance. To provide HUD some assurance that MAP Lenders and Underwriters are qualified for their responsibilities, MAP requires Lenders and Underwriters to be approved by LQMD.

B. Approval of a MAP Lender or Underwriter by LQMD is on a nationwide basis, so that the MAP Lender or Underwriter may process MAP loans regardless of which Hub or Program Center will be processing the loan. By accepting the opportunity to use MAP, a MAP Lender and Underwriter agrees that its MAP loans will be subject to post-endorsement review by the LQMD and that if it fails to meet HUD standards for underwriting loans, its MAP designation may be terminated. MAP approval does not expire but may be terminated in accordance with the Quality Assurance Enforcement Actions in Chapter 15.

C. Approval by LQMD as a MAP Lender or Underwriter is a prerequisite to participation in the MAP program, but MAP approval does not obviate the need to have an experienced team on each application. If the HUD office has concerns regarding the Underwriter's or Lender's past performance or capabilities, the office should consult with LQMD for potential enforcement actions.

   Refer to Chapter 1 for specifics on third party consultant approvals. The Lender is responsible for insuring that all third party contractors meet the requirements outlined in the Map Guide, including the USPAP Competency provision and jurisdictional certification requirements. The names and resumes of the appraiser and market analyst should be submitted as soon as possible prior to the Pre-application. The names of the architectural analyst and cost analyst should be submitted prior to the application for a Firm Commitment. For refinancing or purchase, the appraiser's resume should also be submitted prior to the application for the Firm Commitment. If the HUD office has concerns regarding the third party contractor's past performance or capabilities, the office should consult with LQMD for potential enforcement actions.

D. Sections 2.2 – 2.7 cover the requirements imposed on Lenders to qualify to submit applications as MAP Lenders. Sections 2.8 – 2.9 discuss the post-endorsement monitoring of MAP loans.

E. The originating MAP Lender may sell or transfer a MAP application only upon receipt of a Firm Commitment. The application may only be sold to another MAP approved Lender not currently subject to any suspension or Limited Denial of Participation penalties.

2.2 Lender Qualifications

A. Lender MAP approval requests should be sent to:

Lender Qualifications and Monitoring Division
Office of Multifamily Development
Room 6138
451 7th Street, SW
Washington, DC 20410
FAX Number: 202-401-9087

B. The Lender prepares the application for approval as a MAP Lender. There is no required form for this application. Upon receipt of all the information specified in Section 2.7, LQMD will process the application within 30 days.

C. The Director of the Office of Multifamily Housing Development will approve in writing each MAP Lender. The names of approved Lenders will be posted by LQMD on the HUD website at: http://www.hud.gov/utilities/intercept.cfm?/offices/hsg/mfh/map/aprvlend.pdf, and for the HUD staff at: http://hudatwork.hud.gov/po/h/hm/fog/dev/authsign.pdf

D. LQMD may disapprove an application on the grounds that: a) it fails to meet the standards set forth in Section 2.3, b) it fails to provide sufficient information required by Section 2.7 or, c) there are specified deficiencies that must be corrected. An appeal of LQMD's decision to disapprove an application may be made to the Deputy Assistant Secretary for Multifamily Housing.

E. If the Lender's approval has been terminated, the Lender may not reapply for 12 months after termination. (See Chapter 15, Section 15.8.E) The Lender may appeal its termination as provided in Chapter 15, Section 15.15.

2.3 Standards Required for Qualification

To qualify as a MAP Lender, it requires evidence that the Lender is an FHA approved multifamily mortgagee, that it is financially sound, that it has on staff principal employees with multifamily underwriting experience, and that its record with FHA-insured or conventional multifamily loans has been satisfactory. The requirements are discussed in this Section and the required application exhibits are listed in Section 2.7, Application Package.

A. A Lender must submit a copy of the approval letter they received that states they are an FHA-approve multifamily mortgagee as a result of submitting Form HUD-92001-B, Branch Office Notification Title I/ Title II.

B. The Lender must not be subject to judgments in administrative claims or in lawsuits, which would seriously affect its ability to do business and must not unlawfully discriminate. Section 2.7 requires the Lender to report any lawsuits or judgments against it within the past three years including any for discrimination in employment or in lending practices.

C. Multifamily underwriting experience on staff is a key to MAP approval. The Lender must identify staff persons with at least three years of recent experience in multifamily underwriting. Over the three years, the Underwriter must have worked regularly in the multifamily lending business and have underwritten at least three loans, which have been funded. The Underwriter must attend a MAP training session conducted by HUD before submitting an application or Pre-application. An FHA mortgagee will not get MAP approval when it hires a multifamily underwriter on a contract basis for a particular loan application. MAP training will be held quarterly by HUD Headquarters, and intermittently by the local Hubs and Programs Centers. When HUD Headquarters is advised by a Hub or Program Center of any training, it will be posted on the MAP home page website under MAP Underwriting training at http://www.hud.gov/offices/hsg/mfh/map/maptraining.cfm.

D. In connection with its application showing experience of staff, the applicant must identify those persons who have the authority to underwrite loan applications and sign the narrative summary in a loan application. The applicant must also describe the ownership of the Lender and identify whose signatures may bind the Lender for its responsibilities under MAP.

E. FHA multifamily experience is not specifically required for initial approval as a MAP Lender, but if the Lender lacks FHA experience, additional emphasis will be place on consistent and recent conventional multifamily lending experience. For any loan processed under MAP, the Lender must thoroughly understand FHA requirements for its mortgage insurance programs.

F. An applicant may be rejected for MAP qualification for a recent history of assignments of FHA-insured loans. The reason for any assignments will be subject to the evaluation of LQMD. Causes of assignments are difficult to measure because of the variety of reasons for assignments, such as unpredictable economic changes in the area, inadequate servicing or poor quality underwriting. LQMD will look at any loan which the applicant has underwritten within the previous five years and which, since the loan was endorsed, has been assigned to HUD to determine whether the applicant was at fault in its origination of a loan that did not perform satisfactorily.

G. The applicant will submit a list of the Hubs and Program Centers with which it has worked in the previous two years. LQMD will contact those offices to ascertain their experience with the applicant and the responses will be included in the applicant's file. A pattern of unsatisfactory applications at one or more Hubs or Program Centers may be grounds for rejection of the applicant.

H. It has long been common practice for Lenders to use consultants, individuals and companies, to increase origination and underwriting capacity. The term consultant, as used here, applies to a

mortgage broker, loan correspondent and packager. The roles and relationships a consultant may have under TAP and MAP processing are the following:

1. Under TAP, the consultant may refer new business to a Lender including information supplied by a proposed borrower/sponsor.

   a. The consultant may provide a wide range of additional services to the Lender. Hub/PCs may accept application packages, correspond with and rely on information submitted by the consultant on behalf of the Lender.

   b. The consultant's fee is paid from the mortgagee's fees.

   c. The consultant cannot have any identity of interest with the borrower, sponsor or affiliated entity. HUD may permit an exception to the rule if:

      (1) The consultant's regular business is brokering and processing loans; and

      (2) The relationship is fully disclosed to and approved by HUD before an application for mortgage insurance is submitted.

2. Under MAP, the consultant's sole purpose is to refer new business to a MAP Lender including information supplied by a proposed borrower/sponsor.

   a. The consultant's fee is paid from the mortgagee's fees.

   b. The consultant cannot have any identity of interest with the borrower/sponsor or any affiliated entity.

   c. There is no additional role for the consultant. HUD only accepts application packages from, corresponds with and relies on information submitted by an approved MAP Lender and only deals with employees of the MAP Lender and only accepts documents signed by the MAP Lender from employees authorized to sign for them. MAP Lenders are authorized to hire third party contractors for appraisal, architecture and cost. The MAP Underwriter performs the mortgage credit and real estate underwriting function and must be a full time employee. The third party contractors cannot have any identity of interest with the borrower/sponsor or any affiliated entity.

2.4 MAP Lender In-House Underwriter Approval Requirements

A MAP Lender may train its in-house staff to be new MAP Underwriters. The Lender must establish a written development plan for underwriter trainees that include a combination of commercial/multifamily training courses and on the job experience.

The underwriter trainee must have successfully completed at least three underwriting, finance, appraisal or environmental courses that demonstrate basic understanding of multifamily underwriting

concepts, one of which must be a multifamily/ commercial appraisal course. These courses may be obtained through the American Bankers Association, Institute of Real Estate Management, National Association of the Review Appraisers & Mortgage Underwriters, the Mortgage Bankers Association of America, the Appraisal Institute or any other acceptable training institution such as colleges and universities. Suggested courses include *Commercial Underwriting*, *Understand Your Construction Borrower*, *Analyzing Financial Statements*, *Commercial Real Estate Financing and Valuation*, *Appraisal: Concepts and Applications*, *Appraisal Principles*, *Appraisal Procedures*, *Basic Income Capitalization*, *Advanced Income Capitalization*, *Uniform Standards of Professional Appraisal Practice (USPAP)*. Architectural and cost knowledge may be obtained through practical experience with the MAP Lender's architectural reviewer or through an acceptable training institution.

In addition to the training courses, HUD requires on the job training of a minimum of three years continuous work experience in multifamily mortgage lending. The underwriter trainee must work on a minimum of three MAP applications that reach Firm Commitment. Only one underwriter trainee may assist the MAP approved underwriter in completion of any MAP application which should document that the trainee was supervised by only one mentor MAP approved Underwriter. The relevant responsibilities are:

A. The MAP approved Underwriter and the trainee must sign the Narrative Summary and the processing forms. An underwriter trainee may assist the Underwriter in completion of the underwriting.

B. The MAP approved Underwriter must accept responsibility for all aspects of the underwriting of the transaction as evidenced by the Narrative Summary and processing forms.

C. The underwriter trainee must be a full time salaried employee of the MAP Lender. The trainee cannot be hired on a contract basis for a particular loan application.

D. If an underwriter trainee contributes to completion of the Underwriter's summary and the processing forms, the trainee's contribution and the specific tasks performed by the trainee should be stated in the Narrative Summary.

E. Work completed by an underwriter trainee must be under the direct supervision of the MAP approved Underwriter and it is unacceptable for the Underwriter to merely sign a form or document prepared by a trainee without providing proper supervision. The mentor Underwriter must add a paragraph in the Underwriter Certification to certify that he/ she has directly supervised the underwriter trainee in completion of the specific tasks in the underwriting narrative and the processing forms. The written request for approval (not by electronic mail) should be submitted by a senior officer of the MAP Lender with signatory authority to LQMD and include:

   1. Written development plan established for the underwriter trainee.
   2. Resume of the underwriter trainee that demonstrates the specific qualifications, education and the level of experience outlined above and a HUD MAP training certificate.
   3. List of MAP loans processed and underwritten by the trainee that reached Firm Commitment, certified and signed by a senior officer with authorized signatory designation and by the underwriter trainee. The list must contain the following warning code:

> **Warning:** *Title 18 U.S.C. 1001, provides in part that whoever knowingly and willfully makes or uses a document containing any false, fictitious, or fraudulent statement or entry, in any manner in the jurisdiction of any department or agency of the United States, shall be fined not more than $10,000 or imprisoned for not more than five years or both.*

a. Complete documentation of each MAP application with the following documentation signed by the trainee and co-signed by the mentor underwriter including:

b. A copy of Underwriter's Narrative that clearly identifies the specific tasks performed by the underwriter trainee.

c. A copy of completed Form HUD-92264-A and other forms and / or exhibits for the type of mortgage proposed that require a mortgage credit analysis. (Refer to Chapter 8 and Appendix 4)

d. A copy of the Master HUD-92264.

e. An Identity of Interest Certification as required by Section 11.2.M, signed and dated by the underwriter trainee only.

F. Underwriter Qualifications and Duties

1. The Lender's underwriter must have knowledge and skills in a variety of financial areas, including:
   a. General experience in banking, accounting, finance, commercial lending, and in multifamily mortgage financing.
   b. The ability to analyze corporate and personal financial statements including, but not limited to, balance sheets, income statements, and statements of changes in financial position and to evaluate the credit acceptability of individuals, partnerships, corporations, and other entities.
   c. A broad knowledge of lending practices for mortgages and construction loans and the financial structures of individuals, partnerships, and other entities.

G. Major Duties and Responsibilities of the Underwriter

The Underwriter serves as the member of the Lender's processing team responsible for mortgage credit analysis. The Underwriter or the Construction Loan Administrator are responsible for management of the Lender's responsibilities during the construction period.

Duties and responsibilities associated with the application underwriting are as follows:

1. Make a determination of the acceptability of the general contractor, the sponsor, the borrower, if formed, and its principals through a thorough analysis of their credit, character, financial condition, and motivation for ownership, availability of assets for closing and adequacy of income for total obligations.

2. Use trade references, bank references, credit data and construction experience resumes in analyzing the construction capability of the general contractor including financial stability, and ability to complete the project and verify other projects in progress.
3. Determine the recommended maximum mortgage amount and other key terms of the loan.

H. Duties and responsibilities of the Construction Loan Administrator during the construction period are:

1. Initial distribution of mortgage proceeds into various accounts and maintain a record of control and disbursement thereafter. This includes the preparation of Form HUD-2283, Financial Requirements for Closing, based on information contained in the Firm Commitment and approved closing documents.

2. Determine construction cost (as approved by the HUD inspector), architect fees and carrying charges payable under request for advances of multifamily mortgage proceeds, prepare written reasons for modifications as necessary.

3. Recommend approval of construction change orders and recommend release of both on-site and off-site escrow funds, citing special requirements or conditions of approval as necessary.

I. Major Duties and Responsibilities of HUD

1. HUD is to perform the following major mortgage credit functions during the application underwriting and construction periods.
   a. During application underwriting:
      (1) Review the Lender's mortgage credit report(s) regarding the acceptability of the sponsor, borrower, and its principals, and the contractor.
      (2) Perform the Active Partner Performance System (APPS) Electronic 2530 Property Submission review.
      (3) Determine the maximum mortgage amount and other key terms of the loan.
      (4) Determine the project's financial feasibility and the acceptability of the market.
      (5) Determine financial settlement requirements.
      (6) Review initial and final closing documents for compliance and acceptability
   b. During the construction period:
      (1) Review and approve the Lender's proposed initial distribution of mortgage proceeds.
      (2) Approve construction change orders.
      (3) Review the borrower's cost certification based on HUD allowed costs.
      (4) Determine the final maximum insurable mortgage.
      (5) Review and approve the final distribution of mortgage proceeds.

2.5 Electronic Capability and Internet Access

HUD will post information on its web site and will transmit messages to Lenders and to the lending community by electronic mail, often with attached documents, Mortgagee Letters, or HUD Housing Notices. Much of the information required by HUD may be submitted electronically.

2.6 Identity of Interest

No financial or family relationship is permitted between an officer, director or partner of the MAP Lender, its principal staff or contract employees working on a particular application and, an officer, director partner or spouse of the sponsor, the borrower, or the principal of the borrower, the general contractor, subcontractor, or the seller of the land or of the property. As used herein, "family relationship" includes, but is not limited to, with respect to any person, his/her spouse, parents, siblings, children, grandparents, grandchildren, aunts, uncles, mother-in-law, father-in-law, brothers-in-law and sisters-in-law. An identity of interest shall be deemed to exist between the Lender and counsel to the Borrower (whether a law firm or an individual attorney), if counsel to the Borrower, or any attorney who is a partner, member or employee of the law firm that is counsel to the Borrower, or any of their family members, is an owner of any direct or indirect ownership interest in Lender or is an employee of Lender. On a LIHTC project, an affiliate of a MAP Lender can be the tax credit equity syndicator or investor and can own up to a 25 percent interest in the 99 percent investor limited partnership entity (or an equivalent percentage if owned as an LLC) of the borrower, under the following conditions:

A. In all instances where there is an identity of interest or affiliation between the MAP Lender and the tax credit equity syndicator or investor: a) the MAP loan must be processed, underwritten and approved by the MAP Lender staff without involvement by the affiliated equity staff, and b) a request for authorization to process the MAP application must be submitted to the Hub or Program Center with jurisdiction for the project, which demonstrates compliance with the following:

   The affiliated tax credit equity syndicator or investor can hold no more than a twenty five (25) percent interest in the limited partnership entity (or an equivalent percentage if owned as an LLC) of the borrower after the project's placed in service date. During the construction or rehabilitation period before the property's placed in service date, the tax credit equity syndicator or investor may make an equity bridge loan to the project that may be evidenced by a promissory note from the sponsor, which may be secured by a pledge of the tax credits or of the limited partnership interest but which may not be secured by a lien on the real estate. After the placed in service date, the affiliated tax credit equity syndicator or investor may not hold an equity bridge loan note and may not own more than a twenty five (25) percent interest in the limited partnership entity of the borrower.

B. HUD must ensure that the affiliated tax credit equity syndicator or investor does not improperly influence the MAP Lender on a LIHTC project. Therefore, the MAP Lender and the affiliated tax credit equity syndicator or investor each must provide the Hub or Program Center a specific Representation and Warranty on each application submitted for a LIHTC project, which contains the following criminal warning language:

   1. The MAP Lender's Representation and Warranty must state:

a. With respect to any LIHTC project loan that it will process under MAP:

(1) No officer or employee of _____ (insert the name of affiliated tax credit syndicator or investor) or any director or parent thereof will have any loan-specific or decision making control or influence in _____'s (insert the name of MAP Lender) underwriting of the MAP loan except by providing factual information to _____ (insert the name of MAP Lender) in the same manner as would be provided by an unaffiliated syndicator).

(2) _____(insert the name of MAP Lender) will not condition its agreement to provide such financing on _____ (insert the name of affiliated tax credit equity syndicator or investor) being selected as the tax credit equity syndicator or investor for the project to be financed by the MAP loan.

b. _____ (insert the name of MAP Lender) will notify HUD promptly, in writing, during application processing of any change or event which causes the foregoing Representation or Warranty to be materially untrue or inaccurate.

2. The MAP Lender's affiliated tax credit syndicator or investor's Representation and Warranty must state:

a. In the regular course of its business it syndicates or invests in tax credit equity investments in multifamily affordable housing projects.

b. With respect to any project loan that is to be underwritten by _____(insert name of MAP Lender) and in which _____(insert name of affiliated tax credit equity syndicator or investor) intends to make an equity investment or sell equity to other investors:

(1) No officer or employee _____(insert name of MAP Lender) will have any loan-specific control or influence in _____'s (insert name of affiliated tax credit equity syndicator or investor) processing of the sponsor's application for tax credit equity syndication or investment except by providing factual information to _____ (insert the name of affiliated tax credit equity syndicator or investor) in the same manner as would be provided to an unaffiliated MAP Lender.

(2) _____ (insert the name of affiliated tax credit equity syndicator or investor) will not condition its commitment to syndicate or invest in the project equity on debt financing for such project being provided by _____ (insert the name of MAP Lender).

(3) Except during the interim period prior to the placed in service date during which _____ (insert name of affiliated tax credit equity syndicator or investor) may make an equity bridge loan to the project, neither _____ (insert the name of affiliated tax credit equity syndicator or investor) nor any affiliate or subsidiary thereof will hold greater than a 25 percent interest in the 99 percent investor limited partnership entity (or an equivalent percentage if owned as an LLC) of the borrower.

C. The Representations and Warranties must include the following criminal warning language: **WARNING**: *"HUD will prosecute false claims and statements. Convictions may result and/or civil penalties. (18 U.S.C. 1001, 1010, 1012; 31 U.S.C. 3729, 3802)"*

D. Hub or Program Centers cannot waive or modify the above required Representations and Warranties from the MAP Lender and from the affiliated tax credit equity syndicator or investor without first obtaining written permission of the HQ Office of Multifamily Development.

Identity of Interest issues can be complex. If there is a question about whether there is an identity of interest between the Lender and the borrower, contractor, and others, all questions and supporting documentation must be submitted to the following address. HUD Headquarters reserves the right to request additional information before a response is given. Send such requests to:

Director of Multifamily Housing Development, Headquarters
ATTN: Lender Qualifications and Monitoring Division
Office of Multifamily Development
451 7th Street, SW, Room 6138
Washington, DC 20410
FAX Number: (202) 401-9087

2.7 Application Package

There is no required application form for approval as a MAP Lender, but the information submitted should include the following:

A. Exhibit A. Name of applicant, address, employer identification number, contact person or persons, telephone and fax number, e-mail address, branch offices for multifamily business with address, telephone and e-mail address, and the FHA Mortgagee ID Number.

B. Exhibit B. List of names and titles of those who are authorized to bind the Lender in matters involving an application, underwriting and origination of insured mortgages under MAP.

C. Exhibit C. Type of mortgagee (e.g., supervised or non-supervised), type of legal structure (e.g., general corporation, limited liability corporation, partnership, housing finance agency or other), whether the mortgagee is a subsidiary of another company, and if so, identification of the parent company.

D. Exhibit D. Copy of most recent financial statements submitted to HQ Lender Approval Division (not applicable to supervised mortgagees).

E. Exhibit E. Narrative discussion of the applicant's method of operation in multifamily lending. This will include whether it: a) services loans, b) is an originator that sells commitments or loans to others, c) originates and holds loans in its portfolio; d) purchases loans from others and e) has experience in construction loan administration. Also include the number, location and staffing of branch offices it operates, any other information the applicant deems relevant in providing a clear description of its business.

F. Exhibit F. Experience of the applicant in multifamily loan origination, for both conventional and FHA insured loans. List the FHA insured loans for which applicant has received Firm Commitments in the last five years and the number, name, location, original amount, HUD Office where processed and whether the loan is in default has been assigned or an election to assign the loan to FHA has been filed. The extent of conventional lending may be summarized rather than listing each conventional mortgage originated in the last five years. It is important to summarize the extent of conventional multifamily experience, the extent to which construction loan administration was involved and the number and percentage of defaults and foreclosures. List any FHA or conventional loan that was sold since origination and is serviced by another Lender. Report on whether the sold loan is in default, foreclosure or has been assigned to FHA. Default for these purposes means a loan whose payment is more than 60 days overdue.

G. Exhibit G. Narrative discussion explaining any elections to assign FHA loans for insurance benefits for any Initial Endorsements that occurred after May 1, 1995.

H. Exhibit H. Resumes of the staff that will be responsible for the submission of MAP loan applications, which demonstrate that the staff has the required multifamily experience.

I. Exhibit I. Experience in construction loan administration, if intending to perform this function. Identify those persons authorized to sign advances, construction change orders and escrow releases.

J. Exhibit J. Information regarding:

1. Lawsuits/claims/judgments filed or issued in the last three years against the applicant which:
   a. Concern equal employment or Lender discrimination prohibited by law, or
   b. Are a result of, or might significantly affect, its multifamily lending business.
2. Any criminal or civil charges brought against the applicant related to the mortgage lending business.

K. Exhibit K. Certification by the Lender that it will certify with each Pre-application and application for mortgage insurance that it is in compliance with the identity-of-interest provisions in the MAP Guide which provide that, “No financial or family relationship is permitted between an officer, director or partner of the MAP Lender, its principal staff or contract employees working on a particular application and an officer, director or partner of the sponsor, the borrower, the principals of the borrower, the general contractor, subcontractors or seller of the land or property.”

L. Exhibit L. An agreement that the Lender will open its files and records on FHA applications for monitoring by HUD staff, including by LQMD and the Office of Inspector General.

M. Exhibit M. A Quality Control Plan for underwriting and construction loan administration, if applicable, of insured mortgages processed under MAP.

N. Exhibit N. Copy of Letter of Approval/HUD approval, Form HUD-92001-B, Branch Office Notification Title I/ Title II, evidencing approval as an FHA Approved Multifamily Mortgagee.

2.8 Limitation on Requirements

A. There are no additional capital requirements for MAP Lenders beyond the Department's minimum net worth and liquidity requirements in 24 CFR Part 202.

B. There is no fee required by HUD for qualifying a MAP Lender.

C. MAP Lenders need to notify LQMD if there has been a change in approved signatories. MAP Lenders are expected to maintain the level of experience and experienced staff members. Other than Underwriters, Construction Analyst, and Administrators, LQMD does not approve or disapprove of individuals working for MAP Lenders.

D. MAP Lenders must notify LQMD if there has been a change of address of the home office for multifamily business, electronic mail address, telephone number, ownership or if the Lender has a material change in its way of doing business. Lenders must also notify LQMD if they withdraw as MAP Lenders, even if temporarily.

2.9 Agreement to Accept Monitoring

The applicant for MAP Lender approval agrees that it will make its files and records available to HUD or HUD's authorized contractors for such monitoring of MAP processed loans as HUD determines. The Lender should retain the origination and underwriting files for three years even if the loan has been sold.

2.10 Monitoring by LQMD

A. MAP Lenders are subject to monitoring and periodic on-site reviews by LQMD to verify that:

1. The Lender adheres to all statutory, regulatory and MAP Guide requirements.
2. The Lender's underwriting decisions are consistent with the requirements of the MAP Guide.
3. The Lender's technical processing is consistent with the requirements of the MAP Guide.
4. The Lender has complied with the conditions of the Firm Commitment and the requirements for Initial or Final Endorsement.
5. The Lender has complied with the requirements for construction loan administration in the MAP Guide.

B. LQMD will not commence reviews of origination and underwriting documentation until after the Lender's first MAP Firm Commitment has been issued. Please note that LQMD reserves the right to review any loans.

C. If a Lender, or an authorized employee or agent of the Lender acting under the control and supervision of the Lender, commits fraud or misrepresentation, HUD reserves its rights to take action against the Lender under the contract of mortgage insurance and Mortgagee Review Board requirements.

D. The review by LQMD is not a substitute for other periodic audits and reviews by HUD, including a financial management review and a review of the Lender's quality control plan as required by HUD Handbook 4060.1 "Mortgagee Approval Handbook."

Chapter 3

Multifamily Mortgage Insurance Programs Eligible for MAP Processing

3.1 Introduction

This chapter contains the basic requirements for the mortgage insurance programs for which Lenders can submit Pre-applications and applications for Firm Commitment.

3.2 General

The following requirements apply to *all* mortgage insurance programs:

A. Regulatory Agreement. All borrowers must execute a HUD Regulatory Agreement governing the operation of the project which will be recorded at Initial Endorsement. Certain parties, as identified by HUD in the Firm Commitment, will be required to sign, within the Regulatory Agreement, an acceptance and acknowledgement of certain personal liability that could arise from bad acts or malfeasance.

B. Single Asset Entity. The mortgaged property must be the only asset of the borrower and there may not be more than one borrower. Natural persons or Tenants-in-Common ownership structures are not permitted. Waiver authority is reserved for the Director, Office of Multifamily Development and must be obtained prior to a Hub/ PC accepting an application for mortgage insurance which does not conform to these prohibitions.

C. Non-recourse. The HUD mortgage note will contain a non-recourse provision as to the mortgagor entity, provided that certain parties may be held personally liable to the extent of losses arising from certain bad acts and malfeasance, as set forth in the Regulatory Agreement. HUD will select such parties based upon their control of the Borrower and their capitalization and assets, in HUD's discretion. Such parties will be identified in the Firm Commitment, and will be required to sign the liability acceptance and acknowledgement provision in the Regulatory Agreement.

D. Fixed and Split interest rate. The interest rate on a HUD insured loan is negotiated between the borrower, the mortgagee and the GNMA investor and must be fixed for the term of the mortgage starting at Initial Endorsement for Insurance of Advances cases, and at the start of construction for Insurance Upon Completion cases. Any change in the mortgage amount due to a change in interest rate must be reflected in an amendment to the Firm Commitment before Initial Endorsement. The newly adopted Note, HUD-94001M, now contains an alternative allowing for split interest rates for the construction and permanent financing periods.

E. Amortization plan. All HUD insured mortgages must amortize through a level annuity monthly payment plan (LAMP), which requires equal monthly payments of principal and interest. LAMP

variations are permissible for transactions involving bond financing and/or tax abatement with HUD approval.

F. HUD application fee. An application for Firm Commitment must include an application fee equal to $3 per $1,000 (30 basis points) of the requested mortgage amount. Market rate project Pre-applications must pay a non-refundable 15 basis point review fee, which fee will be credited to the 30 basis point Firm Commitment fee if an invitation letter is issued and a Firm Commitment application is submitted. Affordable housing projects that submit for two stage processing must pay the 30 basis point fee at the Firm Commitment stage, but will not be charged a fee for Pre-application review.

G. HUD inspection fee. The HUD inspection fee is $5 per thousand of the mortgage amount for new construction and $5 per thousand of improvement costs for substantial rehabilitation. For loans insured pursuant to Section 207/223(f) or 223(a)(7), the inspection fee is the following:

1. $30 per unit where the repairs/improvements are greater than $100,000 in total but $3,000 or less per unit.
2. $30 per unit or 1% of the cost of repairs, whichever is greater, where the repairs/improvements are more than $3,000 per unit.
3. $1,500 where the repairs/improvements are less than $100,000, which fee may be waived by the Hub/PC.

H. Mortgage insurance premium. The construction period and annual mortgage insurance premiums (MIP) are based on a percentage of the mortgage amount and may vary, depending on the insurance program and on the MIP schedule posted by HUD each fiscal year. The initial premium is payable in advance at Initial Endorsement.

I. Lender fees and charges. The maximum financing fee the Lender may charge is 3.5% of the mortgage amount. Financing fees up to 5.5% are permissible in bond transactions. Third party costs may be included as mortgagable soft costs in the mortgage calculations. Include third party costs, e.g., appraisal, market study, PCNA, with other organization costs, if any, in Section G., line 65 of Form HUD-92264 and these costs may be included in the calculation of BSPRA where applicable. The Lender's third party expenses, including borrower's organization costs, are exempt from the 65% Initial Endorsement disbursement rule. See Section 11.4 for additional provisions regarding loan fees and charges.

J. Fair Housing and Equal Opportunity. Borrowers, management agents, contractors and subcontractors must comply with HUD Fair Housing and Equal Opportunity requirements, including selection of occupants, employment, and project accessibility (See 24 CFR Part 100 and subsequent Sections), "Affirmative Fair Housing Marketing" (24 CFR Part 200.600 and Handbook 8025.1 Revision 2), and "Nondiscrimination Based on Handicap in Federally Assisted Programs and Activities of the Department of Housing and Urban Development" (24 CFR Part 8).

K. Previous Participation. All principals in the proposed transaction must submit information regarding previous participation in governmental housing transactions either via the electronic

Active Partner Participation System (APPS) or on Form HUD-2530 for approval for participation in any mortgage insurance program.

Invitation Letters or Firm Commitments may be issued conditioned on 2530/APPS approval, assuming no critical findings and that the 2530 flags can be resolved without being presented to the Multifamily Participation Review Committee.

L. Age Discrimination in Occupancy. Except in the case of a project designed exclusively for the elderly (age 62 and over), the borrower must certify that it will not discriminate based on age or against families with children. HUD does not permit projects with occupancy restricted to age 55 and older under any of the MAP Guide programs; this provision shall not be waived except by the Headquarters' Office of Multifamily Development.

M. HUD's Fiscal Procedures are contained in HUD Handbook 4410.1 Revision 2.

N. Bridge or Gap Financing. Bridge financing is a loan that is secured by the property, or by a pledge of an interest in the borrowing entity, covering the period between the termination of a short-term financing and the start of a long-term permanent loan. Bridge loans that are secured by the property (as distinguished from a tax credit equity bridge loan which is secured by the ownership interest and by a pledge of future tax credits), are acceptable only in instances of Insurance Upon Completion and before the start of the FHA-insured permanent financing. Bridge financing is permitted so long as the bridge loan is repaid at the time of permanent loan closing and any bridge loan debt is not intended to increase the FHA insured mortgage or circumvent outstanding program requirements. Gap financing is a loan that is secured by a subordinate lien behind the permanent first mortgage to provide additional capital funds for the project. Gap financing is generally only permitted for affordable housing transactions where the gap lender is a governmental agency and it must otherwise meet the Guide's requirements for secondary financing.

O. Transient Housing/Hotel Services Prohibition. Section 513 of the National Housing Act prohibits the use of the insurance programs for transient or hotel purposes. Leases for less than 30 days are prohibited and occupants cannot be provided with hotel services such as maid service, furnishing and laundering of linens, room service and bellboys, and also applies to any commercial space funded by the mortgage.

P. Operating Deficit. An operating deficit escrow is required on all applications for new construction and substantial rehabilitation to provide funding for operating expenses and debt service when net income is not available during the initial lease up and stabilization period. A debt service escrow may also be required on Section 223(f) proposals where analysis requires it. This escrow is not mortgageable and unused portions will be returned to the Borrower.

Q. Definition of Affordable Housing.

1. Affordable housing is defined as projects meeting all of the following requirements: (a) projects that have a recorded regulatory agreement that will be in effect for at least 15 years after Final Endorsement, (b) projects that meet at least the minimum LIHTC restrictions of 20% of units at 50% of area median income (AMI), or 40% of units at 60% of AMI, with economic rents (i.e. the portion paid by the residents) on those units no greater than LIHTC

rents; and (c) mixed income projects if the minimum low income unit rent and occupancy restrictions and regulatory agreement meet the above criteria.

2. Projects need not use LIHTCs to qualify for affordable underwriting so long as they have, and are in compliance with, a recorded Regulatory Agreement imposing the minimum low income occupancy and restricted rent tests above, with a term of at least 15 years after Final Endorsement. The recorded regulatory agreement must be imposed, monitored and enforced by a governmental agency. *An "affordable project" does not need to have actual LIHTCs so long as a recorded Regulatory Agreement is in place for the term specified, that meets or exceeds the rent and income limitations for the LIHTC program*.

R. Short-Term Lease Premiums. Projects that provide leases with terms that are less than 30 days are not eligible for HUD-insured financing under any circumstances. Treatment of income from other short-term leases, i.e., furnished units, corporate or business short term leases may be considered to the extent that it is present in the local market. The actual number of furnished or corporate/business units must be approved by Asset Management. For short term lease underwriting and valuation instructions, i.e., percentage of gross income limitations, disallowance of short term lease premiums to derive project net operating income and other requirements, see Section 7.7.M, Valuation Analysis.

S. Replacement Reserve. A replacement reserve is a set aside from project operating income to pay for the eventual replacement of short-lived physical assets. See Section 7.8 for the minimum annual replacement reserve requirements for all program types and Appendix 5M for guidance on completing a Project Capital Needs Assessment (PCNA) for all insured projects every 10 years. See Handbook 4350.4, Chapter 2 Servicing Manual, on the Lender's responsibility on managing funds held for the project that describes the liquidity, draws and investment requirements.

T. Condominiums. A project which was built and plotted as condominiums, but is now operating as a rental project, may be considered under Section 223(f) if the condominium regime is converted to a single owner with no individual unit ownership and the property meets the other program guidelines, including the minimum occupancy standards. Condominium regimes are similarly permitted under new construction and substantial rehabilitation proposals that meet these same requirements.

Condominium ownership regimes and plots may be recorded if the property is otherwise operated as a rental project with a single ownership entity owning all the apartments. Separate condominium units may be established for commercial use and for housing use which must include all the residential apartments. The insured loan must be secured by a mortgage on the rental apartment portion and any mortgagable commercial space. Joint use and maintenance agreements and easements between the insured portion and any separately demised condominium portion must be defined.

The Hub/PC Director may consider a waiver for a condominium building with a limited number of individually owned units (i.e.: 10% or less of total units) if all the owned units are located in a separate building or in a separate section of a single building apart from the rental units. HUD will not consider a waiver if any ownership units are interspersed with the rental units.

U. Environmental Review. HUD has responsibilities to comply with various environmental laws and regulations and imposes submission requirements on Lenders to assist in this review, which is detailed in Chapter 9, Environmental Review.

3.3 New Construction/ Substantial Rehabilitation Multifamily Rental Apartments: Eligible Programs – Sections 220, 221(d)(3), 221(d)(4), and 231

Lenders must submit requests for a concept meeting, Pre-application review and Firm Commitment applications under the programs listed immediately below for new construction and substantial rehabilitation proposals.

Housing Act	General Borrower Types for Eligible Programs
Section 220:	profit-motivated, public body, limited distribution
Section 221(d) (3):	private nonprofit, public body, limited distribution
Section 221(d)(4):	private nonprofit, profit motivated, public body
Section 231:	private nonprofit, public body, profit-motivated

3.4 New Construction/Substantial Rehabilitation Rental Properties: Requirements and Program Features

A. HUD will insure loans on properties 5 or more residential units with complete kitchens and baths for both the construction and permanent loan periods (called Insurance of Advances) or for just the permanent loan period (called Insurance Upon Completion).

B. New construction of improvements where no work has been done to the site prior to Initial Endorsement:

   1. Work can begin after issuance of a Firm Commitment with specific approval from the Hub/PC using the Early Construction Start process in Chapter 5 Section 5.7.
   2. Construction may not start on Insurance Upon Completion projects until issuance of a Firm Commitment.

C. Substantial Rehabilitation. A property qualifies if it meets one of the following criteria:

   1. The cost of repairs, replacements and improvements exceeds the *greater* of 15% of the estimated property replacement cost after completion of all repairs, replacements and improvements, or $6500 per unit in repairs, replacements and improvements as adjusted by the Hub/PC high cost percentage for that area, *or*

2. Two or more major building components are being substantially replaced. Additions are permitted in substantial rehabilitation projects, but the costs for the additions of new units (not building component additions) are *not* included in the eligibility test.

D. Loan Terms. The maximum loan term is 40 years for new construction/substantial rehabilitation, 35 years for purchase/refinancing, or 75% of the remaining economic life of the property, whichever is less. See Section 8.5.

E. Prepayment Restrictions.

HUD permits, but does not impose, prepayment restrictions on insured loans. Prepayment restrictions cannot require that HUD consent to prepayment of the loan by the borrower.

1. Form HUD-94001M, Note, includes alternate provisions regarding prepayment restrictions that should be used or stricken as applicable. In all instances involving non-HUD imposed prepayment requirements, HUD consent for prepayment cannot be included in the Note and this provision cannot be waived except by Headquarters' Office of Multifamily Development. See Section 11.7.B.2 for prepayment restrictions imposed on certain nonprofit borrowers under certain HUD programs.
2. Where obligations pursuant to tax-exempt bond financing or GNMA involvement do not impose restrictions independent of the Lender's restrictions, HUD may consider exercising an override of prepayment lockout and/or premium provisions imposed by the Lender if:
   a. Borrower has defaulted on the insured loan and HUD has received notice as required by the regulations;
   b. HUD determines that the project has been experiencing a net income deficiency, which has not been caused solely by management inadequacy or lack of owner interest, and which is of such a magnitude that the mortgagor is currently unable to make required debt service payments on the insured loan, pay all project operating expenses and fund all required HUD reserves;
   c. HUD finds there is a reasonable likelihood that the Borrower can arrange to refinance the defaulted loan at a lower interest rate or otherwise reduce the debt service payments through partial prepayment; and
   d. HUD determines that refinancing the defaulted loan at a lower rate or partial prepayment is necessary to restore the project to a financially viable condition and to avoid a full insurance claim.
3. If an event of default occurs during a period in which prepayment may not be made or may not be made without a penalty of one percent or less, Lender must:
   a. request a 3-month extension of the deadline prescribed by 24 C.F.R. Section 207.258 for filing a notice of its intention to file an insurance claim and its election to assign the mortgage;
   b. assist the Borrower to arrange refinancing to cure the default and avert an insurance claim if HUD grants the requested (or shorter) extension of the notice filing deadline;
   c. report to HUD at least monthly on any progress in arranging a refinancing;
   d. otherwise cooperate with HUD in taking reasonable steps to avoid an insurance claim;

e. require any successors or assigns to certify in writing that they agree to be bound by these conditions for the remainder of the term of the prepayment lockout and/or penalty period; and

f. notify HUD of the delinquency where a payment is not received by the 16th day of the month in which it is due.

F. Cost Certification. The borrower must submit a cost certification prepared by an independent CPA upon completion of construction or substantial rehabilitation. The mortgage amount that is finally endorsed for insurance after completion of construction can be reduced based upon HUD review of the cost certified amounts. General contractors or subcontractors are required to submit a cost certification if there is an identity of interest with the borrower. See Chapter 13 for tax credit project cost certification procedures.

G. Federal Labor Standards. The general contractor and all subcontractors are required to comply with federal wage and reporting requirements, including the payment of prevailing wage rates and the submission of weekly certified payroll reports. Prevailing wage schedules may be obtained from the Hub/PC.

H. Liens/Secondary Financing. HUD insured mortgages must be first liens. Secondary liens are permitted in the case of HUD insured second mortgages (supplemental loans and operating loss loans) and other governmental loans, in accordance with Chapter 8's requirements for secondary financing.

I. Commercial Space. Commercial facilities may be included in a mixed use project, subject to programmatic space and income limitations. See Section 3.7 for further guidance.

J. Military Impacted Areas. HUD may not insurance mortgages in military impacted areas unless HUD determines that demand from nonmilitary households is sufficient to sustain occupancy in both the insured project and the market as a whole. Section 238(c) of the National Housing Act authorizes the provision of insurance in military impacted areas upon certain findings by the Department of Defense (DOD) and HUD HQ. In such areas, borrowers should be encouraged to contact DOD for other potential programs administered by DOD which could provide alternative sources of financing for the proposed project. Section 238(c) loans are not eligible for MAP but may be processed under TAP.

K. Student Housing. Insured projects cannot be designed solely for student occupancy, although students and families are eligible occupants of insured family housing projects. Insured loans on projects in college areas must be underwritten at rents that are comparable to family housing in the area. Loans cannot be underwritten with rental rates assuming multiple student occupants in a unit that would result in a processing rent higher than a typical family apartment.

L. Real Estate Requirements. The insured mortgage must be on real estate:

1. Held in fee simple, or
2. Under a lease with a term of 10 years or more than the loan maturity date.

M. Assurance of Completion. The general contractor shall provide an assurance of completion of construction on forms approved by HUD.

1. For non-elevator buildings, or elevator buildings with three stories or less, where the cost of construction or rehabilitation is more than $500,000, the assurance shall be in the form of corporate surety bonds for payment and performance, each in the amount of 100% of HUD's estimated cost of construction or rehabilitation including an assumed builder's profit on BSPRA transactions (see Section G Line 50, Form HUD-92246, less architect's design and supervisory fee and mortgagor's other fees). Alternatively, the completion assurance agreement may be secured by a cash deposit or Letter of Credit in the amount of 15% of the HUD estimated cost of construction or rehabilitation.
2. For elevator buildings of four (4) stories or more, the assurance shall be in the form of corporate surety bonds for payment and performance, each in the amount of 100% of HUD's estimated cost of construction or rehabilitation including an imposed builder's profit on BSPRA transactions. Alternatively, the completion assurance agreement may be secured by a cash deposit or Letter of Credit in the amount of 25% of the HUD estimated cost of construction or rehabilitation.

N. Underwritten Occupancy. The maximum physical occupancy percentages for underwriting new construction and substantial rehabilitation or refinancing projects are provided in Section 7.6.A.7.

O. Absorption Period. The absorption period used in estimating market demand for proposed newly constructed or substantially rehabilitated units is 18 months. Larger projects may phase additional units under a separate application for mortgage insurance. An exception to the 18 month limitation on the absorption period may be considered by the Hub/PC Director for large high rise buildings which will be evaluated based on their own merit and will require a larger initial operating deposit.

P. Marketing, Leasing and (if applicable) Relocation Plan. All projects which require absorption of units at economic rents to achieve break-even occupancy must submit a detailed marketing and leasing plan and budget that has been reviewed and confirmed by the proposed property management company. The plan must discuss when marketing efforts will begin, when the leasing office and model units will be opened, how the leasing office will be staffed, and the project's marketing and advertising strategy. The plan must address timing of the construction progress schedule with respect to egress and ingress into the project, landscaping and access to amenities. These items are in addition to those required by the Affirmative Fair Housing Marketing Plan.

   For substantial rehabilitation projects involving temporary relocation or displacement of residents, the plan must address details of timing, funding and management of the relocation process.

Q. Working Capital Escrow. The Working Capital Escrow is designed to cover accruals of taxes, insurance, and interest in the case of construction delay, construction contingencies for cost overruns and change orders, and other miscellaneous expenses which are not included in the mortgage and is required for new construction and substantial rehabilitation proposals. See Section 8.13 for general requirements and Section 12.15.C for working capital escrow release instructions.

R. Furniture, Fixture and Equipment (FF&E) in Cost Basis. Reasonable costs of Furniture, Fixture and Equipment may be included in mortgagable project costs and in the Reserves for Replacement

for new construction and substantial rehabilitation proposals. See Chapter 6 Section 6.3 for FF&E examples and guidance. All funded FF&E will be subject to HUD's security instruments.

S. Elderly Developments. New construction or substantial rehabilitation of apartments specifically designed for the elderly age 62 and over, as defined by the National Housing Act, should be processed under Section 231 which allows a project to restrict its use and occupancy to elderly residents only. HUD requires that, so long as a head of household or their spouse are age 62 or over, other persons less than age 62 including children under age 18, may not be prohibited from living in the unit, based exclusively on their age.

1. Projects with extensive service packages or otherwise specifically designed for elderly occupancy such that all or a portion of the units would be eligible under Section 232 of the National Housing Act are not eligible for MAP insurance programs. The following are typical Section 232 project characteristics that <u>are not</u> eligible for processing as MAP elderly housing developments:

   a. Project such as nursing homes, intermediate care facilities, board and care homes, assisted living facilities and day care in eligible health care facilities as defined under Section 232, or projects that contain comparable characteristics.

   b. Projects in which any percentage of the units must be licensed or regulated by the state or municipality in which the facility is located, other than a standard rental housing occupancy or operating license.

   c. Projects in which the borrower is required to obtain a Certificate of Need or comparable documentation from the state or municipality.

   d. Elderly housing developments that provide "continuous protective oversight" services for residents in the manner defined under Section 232.

   e. Residential accommodations including: a) programmatic restrictions on the number of bedrooms per unit from efficiency through 3 bedroom units, b) non-self contained units, i.e., a bathroom shared by different residents, or c) a kitchenette or less than what would constitute standard, full kitchen equipment.

   f. Mandatory resident meal requirements.

   g. Other resident services made a mandatory condition of occupancy.

   h. Non-shelter and optional services included in the underwriting of net operating income.

2. Meals Service Exceptions.

   a. Refinancing Section 202 and 202/8 direct loan prepayments under Sections 221(d)(3), 221(d)(4) and 223(f).

      By final rule published in 56 FR 42798, central kitchens and the provision of food services in elderly housing projects are prohibited under any rental housing section of the National Housing Act, including Sections 223 (f), 221(d)(3) and 221(d)(4). The Hub/PC Director may permit meals to be served in refinanced Section 202 projects if:

      1. Meals were provided before September 30, 1991 (the effective date of the regulation) and have been continuously provided since that date;

2. Income and expenses from the meal service are not included in the underwriting of net operating income; and
3. The cost of the meals program is self-sustaining by the revenue it generates based on HUD's review of the project's financial statements.

b. Non-shelter spaces already constructed for projects with current insured mortgages may include formal dining areas with meal services if they are provided to residents on an optional basis.

3. Prohibition on Founder's Fees. "Founders' Fees," "admission fees," or similar types of initial occupancy or entry payments are prohibited.

T. Occupancy Preference. Sponsoring nonprofit organizations such as labor unions, professional groups, religious organizations and fraternal or civic organizations, may give preference to their members, provided membership in the organization is open without regard to race, color, national origin, sex, sexual orientation, disability or religion. However, sponsors cannot restrict occupancy solely to their members.

U. Builder and Sponsor's Profit and Risk Allowance (BSPRA) and Sponsor's Profit and Risk Allowance (SPRA) are allowed for new construction and substantial rehabilitation applications under Sections 221(d)(3), 221(d)(4), 220 and 231 for profit motivated and limited distribution borrowers. Non-profit borrowers are eligible for a developer's fee as provided in Chapter 8.

1. The BSPRA allowance will be credited against the borrower's required equity contribution. To use BSPRA, there must be an identity of interest between the borrower and general contractor and there must be no paid builder's profit contained in the mortgage calculation. For new construction, BSPRA is 10% of the estimated cost of: on site improvements, structures, general requirements, general overhead, architect's fees, carrying charges and financing, legal, organizational and audit expenses (total of lines 50, 63 and 67 in Section G. of Form HUD-92264), exclusive of land. For substantial rehabilitation projects, BSPRA is 10% of the above costs exclusive of the as is value of the existing structure.
2. SPRA will be included in replacement cost where no identity of interest exists between the general contractor and borrower. SPRA is 10% of the total estimated cost of: architect's fees, carrying and financing charges, legal, organizational, and audit expenses.

V. Energy Efficiency. New construction or substantial rehabilitation projects must comply with the International Energy Conservation Code (IECC) 2006, or in the case of multifamily high rises, ASHRAE Standard 90.1-2004, or applicable successor codes [as adopted by the Secretary pursuant to the requirements of the Energy Independence and Security Act of 2007, Public Law 110-140].

3.5 Section 221(d)(4) New Construction and Substantial Rehabilitation

Section 221(d)(4) insures mortgages for the new construction or substantial rehabilitation of rental housing for families, the elderly and the handicapped. In addition to the general requirements in Sections 3.2, 3.3, and 3.4, the following requirements apply to Section 221(d)(4):

Maximum Loan Ratios and Debt Service Coverage Ratios. The following loan ratios and percentages are required to complete the Form HUD-92264-A, Supplement to Project Analysis, mortgage criteria. The lowest of the mortgage criterion controls the loan amount. See Chapter 8, Mortgage Credit Underwriting and Processing Requirements, for more complete form instructions.

Section 221(d)(4)

New Construction and Substantial Rehabilitation

Criteria 1:

Loan Amount Requested in the Application. The requested application amount may be amended when appropriate, e.g. when a higher mortgage is supportable due to a drop in rates.

Criteria 3:

Amount Based on Replacement Cost: The applicable percentage of the estimated replacement cost for new construction or the applicable percentage of the sum of the estimated replacement cost for substantial rehabilitation plus the "as is" value of the property before substantial rehabilitation is:

a. 90% - for projects with 90% or greater rental assistance;
b. 87% - for projects that meet the definition of Affordable Housing; or
c. 83.3% - for market rate projects

Criteria 4:

Amount Based on Limitations per Family Unit: Where percentages are required, enter the same percentage applied under Criteria 3. See Chapter 8 for complete details and the MF Housing website: http://www.hud.gov/offices/hsg/mfh/hicost/hicost.cfm on information for per family unit limitations and the High Cost Percentage by jurisdiction.

Criteria 5:

Amount Based on Debt Service Ratio (DSCR) (ratios are rounded for presentation purposes):

a. 90% (1.11 DSCR) – for projects with 90% or greater rental assistance;
b. 87% (1.15 DSCR) – for projects that meet the definition of Affordable Housing; or
c. 83.3% (1.20 DSCR) - for market rate projects

Criteria 11: See Chapters 8 and 14 for details.

3.6 Section 221(d)(3) New Construction and Substantial Rehabilitation

Section 221(d)(3) insures mortgages that facilitate the new construction or substantial rehabilitation of rental housing for low and moderate-income families, the elderly, and the handicapped and is only available when credit subsidy is available and has been reserved by HUD at the time of application submission.

In addition to the general requirements in Sections 3.2, 3.3, and 3.4, above, the following requirements apply to Section 221(d)(3):

A. Nonprofit sponsor/borrower. Section 221(d)(3) insured loans are limited to nonprofit borrowers, defined as corporations or associations organized to fulfill public purposes and to operate other than for profit or gain, and which HUD finds are not controlled by a profit motivated persons or firms. Generally, borrowers must be qualified under Chapter 501(c)(3) of the Internal Revenue Code. HUD will review the relationships between the nonprofit borrower and the for-profit entities in the transaction and will not insure transactions unless the nonprofit has the financial capacity and experience to own and operate the project independently.

B. Maximum Loan Ratios and Debt Service Coverage Ratios (DSCR). The following loan ratios and percentages are required to complete the Form HUD-92264-A, Supplement to Project Analysis, mortgage criteria. The lowest of the mortgage criterion controls the loan amount. See Chapter 8, Mortgage Credit Underwriting and Processing Requirements, for more complete form instructions.

Section 221(d)(3)

New Construction and Substantial Rehabilitation

Criteria 1:

Loan Amount Requested on Application. The requested application amount may be amended when appropriate, e.g. when a higher mortgage is supportable due to a drop in rates.

Criteria 3:

Amount Based on Replacement Cost: The applicable percentage of the estimated replacement cost for new construction or the applicable percentage of the sum of the estimated replacement cost for substantial rehabilitation plus the "as is" value of the property before substantial rehabilitation.

a. 90% - for projects with 90% or greater rental assistance;

b. 90% - for projects that meet the definition of Affordable Housing; or

Criteria 4:

Amount Based on Limitations per Family Unit: Where percentages are required, enter the same percentage applied under Criteria 3. See Chapter 8 for complete details and the MF Housing website: http://www.hud.gov/offices/hsg/mfh/hicost/hicost.cfm on information for per family unit limitations and the High Cost Percentage by jurisdiction.

Criterion 5:

Amount Based on DSCR (ratios are rounded for presentation purposes):

a. 90% (1.11 DSCR) – for projects with 90% or greater rental assistance
b. 90% (1.11 DSCR) – for projects that meet the definition of Affordable Housing

Criteria 11: See Chapters 8 and 14 for details.

D. Prepayment. A Section 221(d)(3) mortgage with a nonprofit borrower cannot be prepaid in full without the prior approval of HUD.

3.7 Section 220 New Construction and Substantial Rehabilitation

Section 220 insures mortgages for mixed use housing projects in urban renewal areas, code enforcement areas and other areas where local governments have undertaken designated revitalization activities.

In addition to the general requirements in Sections 3.2, 3.3, and 3.4, the following requirements apply to Section 220:

A. Eligible Areas. The property must be located in one of the following:
   1. Existing slum clearance and urban redevelopment projects covered by a Federal aid contract before the effective date of the Housing Act of 1954.
   2. An approved urban renewal area under Title I of the Housing Act of 1949.
   3. Disaster urban renewal projects assisted under Section III of the Housing Act of 1949 as amended.
   4. An area of concentrated code enforcement being carried out under Section 117 of the Housing Act of 1949.
   5. A concentrated development area, approved by the Hub/PC, in which concentrated housing, physical development and public service activities are being carried out in a coordinated manner, pursuant to a locally developed strategy for neighborhood improvement, conservation or preservation. The locally developed strategy shall:
      a. Provide for a combination of physical improvements, necessary public facilities and services, housing programs, private investment and citizen self-help activities appropriate to the needs of the area;
      b. Coordinate public and private development efforts;
      c. Provide sufficient resources to produce substantial long-term improvements in the area within a reasonable amount of time, taking into account the severity of the area's problems.

B. Commercial Facilities. Commercial space may be included if it will serve the needs of the project residents and other residents of the area. Commercial space is limited to 20% of total net rentable area and commercial income to 30% of effective gross project income.

   Section 220 projects with the maximum commercial space or commercial income allowed by the program must be underwritten based on the Section 221(d)(4) market rate DSCR and replacement

cost loan ratios, even if all or some of the housing units are affordable. Section 220 projects with both commercial space and income less than the maximum allowed can be underwritten as affordable if the residential units meet the definition in Section 3.2Q.

See Section 7.7 and Section 7.8 for separate appraisal and market study analysis requirements where commercial facilities are included in a project.

C. Maximum Loan Ratios and DSCRs. The following loan ratios and percentages are required to complete the Form HUD-92264-A, Supplement to Project Analysis, mortgage criteria. The lowest of the mortgage criterion controls the loan amount. See Chapter 8, Mortgage Credit Underwriting and Processing Requirements for more complete form instructions.

Section 220

New Construction and Substantial Rehabilitation

Criteria 1:

Loan Amount Requested on Application. The requested application amount may be amended when appropriate, e.g. when a higher mortgage is supportable due to a drop in rates.

Criteria 3:

Amount Based on Replacement Cost: The applicable percentage of the estimated replacement cost for new construction or the applicable percentage of the sum of the estimated replacement cost for substantial rehabilitation, plus the "as is" value of the property before substantial rehabilitation.

a. 90% - for projects with 90% or greater rental assistance;
b. 87% - for projects that meet the definition of Affordable Housing; or
c. 83.3% - for market rate projects

Criteria 4:

Amount Based on Limitations per Family Unit: Where percentages are required, enter the same percentage applied under Criteria 3. See Chapter 8 for complete details and the MF Housing website: http://www.hud.gov/offices/hsg/mfh/hicost/hicost.cfm on information for per family unit limitations and the High Cost Percentage by jurisdiction.

Criteria 5:

Amount Based on DSCR (ratios are rounded for presentation purposes):

a. 90% (1.11 DSCR) - for projects with 90% or greater rental assistance
b. 87% (1.15 DSCR) - for projects that meet the definition of Affordable Housing; or
c. 83.3% (1.20 DSCR) - for market rate projects

Criteria 11: See Chapters 8 and 13 for details.

D. Builder/Sponsor Profit and Risk Allowance (BSPRA). See definition of BSPRA in Section 3.4.

E. Sponsor Profit and Risk Allowance (SPRA). See definition of SPRA in Section 3.4.

F. Elderly Developments. Apartments specifically designed for the elderly and/or limited to elderly occupancy are not permitted under this Section.

3.8 Section 231 Housing for Elderly Persons – New Construction and Substantial Rehabilitation

A. Section 231 insures mortgages for construction and substantial rehabilitation of rental housing for elderly persons (aged 62 or older) and/or persons with disabilities. A project must comprise 8 or more new or substantially rehabilitated units designed for occupancy by elderly persons and may include family units for occupancy for persons who qualify as handicapped.

All Section 231 Pre-application and Firm Commitment packages -- regardless of loan size or unit count -- must be reviewed by the National Loan Committee (NLC) prior to issuance. Senior housing proposals processed under Section 221(d (4) which also permit elderly living with children, does not require NLC review unless NLC protocol otherwise requires it or there are special risk issues that merit such a review if, for example, there are high-end rents or extensive optional services. Further guidance on senior housing is being developed and will be released in a future notice.

1. Definitions/Explanations of Terms:
   a. Elderly Person. A person aged 62 or older. For Section 231 occupancy, other than for units designed for the use and occupancy of handicapped persons and their families, all persons living in a unit must be age 62 or over.
   b. Handicapped Person. A person who has a physical impairment which:
      (1) Is expected to be of a long-continued and indefinite duration;
      (2) May substantially impede his/her ability to live independently; and
      (3) Is of such a nature that his/her ability to live independently could be improved by more suitable housing conditions.

B. Room Lay Out, Design and Special Amenities. Particular attention is to be given to room lay out ands unit design to assure they are consistent with the needs of the elderly or handicapped market.

C. BSPRA or SPRA allowances are eligible under Section 231. See Section 3.4.U for an explanation of these allowances.

D. Maximum Loan Ratios and DSCR. The following loan ratios and percentages are required to complete the Form HUD-92264-A, Supplement to Project Analysis, mortgage criteria. The lowest of the mortgage criterion controls the loan amount. See Chapter 8, Mortgage Credit Underwriting and Processing Requirements, for more complete form instructions.

<u>Section 231</u>
<u>New Construction</u>

<u>Criteria 1</u>:

Loan Amount Requested on Application. The requested application amount may be amended when appropriate, e.g. when a higher mortgage is supportable due to a drop in rates.

Criteria 3:

Amount Based on Replacement Cost: The applicable percentage of the estimated replacement cost for new construction.

a. 90% - for projects with 90% or greater rental assistance;
b. 87% - for projects that meet the definition of Affordable Housing ; or
c. 83.3% - for market rate projects

Criteria 4:

Amount Based on Limitations per Family Unit: Where percentages are required, enter the same percentage applied under Criteria 3. See Chapter 8 for complete details and the MF Housing website: http://www.hud.gov/offices/hsg/mfh/hicost/hicost.cfm on information for per family unit limitations and the High Cost Percentage by jurisdiction.

Criterion 5:

Amount Based on DSCR (ratios are rounded for presentation purposes):

a. 90% (1.11 DSCR) – for projects with 90% or greater rental assistance
b. 87% (1.15 DSCR) – for projects that meet the definition of Affordable Housing; or
c. 83.3% (1.20 DSCR) - for market rate projects

Criteria 11: See Chapters 8 and 14 for details.

Section 231

Substantial Rehabilitation

Criteria 1:

Loan Amount Requested on Application. The requested application amount may be amended when appropriate, e.g. when a higher mortgage is supportable due to a drop in rates.

Criteria 3:

Amount Based on Value: The applicable percentage of the estimated replacement cost for new construction.

a. 90% - for projects with 90% or greater rental assistance;
b. 87% - for projects that meet the definition of Affordable Housing ; or
c. 83.3% - for market rate projects

Criteria 4:

Amount Based on Limitations per Family Unit: Where percentages are required, enter the same percentage applied under Criteria 3. See Chapter 8 for complete details and the MF Housing website: http://www.hud.gov/offices/hsg/mfh/hicost/hicost.cfm on information for per family unit limitations and the High Cost Percentage by jurisdiction.

Criteria 5:

Amount Based on DSCR (ratios are rounded for presentation purposes):

a. 90% (1.11 DSCR) – for projects with 90% or greater rental assistance;
b. 87% (1.15 DSCR) – for projects that meet the definition of Affordable Housing; or
c. 83.3% (1.20 DSCR) - for market rate projects

Criteria 6:

a. Line 6.f. "As Is" Value of Property Before Rehab is multiplied by the same percentage applied under Criteria 3.
b. Line 6.i. enter 100%.

Criteria 11: See Chapters 8 and 14 for details.

3.9 Section 223(f) Acquisition/Refinancing of Existing Apartments

Section 207/223(f) insures mortgages for the purchase or refinancing of existing rental housing which may have been financed originally with conventional mortgages or equity. Properties requiring substantial rehabilitation are not eligible for this program. HUD requires completion of critical repairs before endorsement of the mortgage and permits the completion of non-critical repairs after endorsement.

In addition to the general requirements in Section 3.2, the following requirements apply to Section 223(f) when used for acquisition or refinancing: 1) Any property acquired by the Borrower before the date of the mortgage insurance application shall be treated as a refinance transaction; 2) Any property acquired the Borrower after the date of the mortgage insurance application shall be treated as a purchase; and 3) In a purchase transaction, any identity of interest, however minor an interest, between seller and purchaser requires the application to be processed as a refinance.

A. Eligible Properties.

The property must contain at least 5 residential units that have been completed or substantially rehabilitated at least 3 years before the date of application. Properties that were constructed or substantially rehabilitated with HUD-insured multifamily mortgages, and the latent defects guarantee period has expired, are exempt from the 3-year rule. Projects with additions completed less than 3 years before the application are eligible for refinancing as long as the size and number of units in the addition are not larger than the size and number of units in the original project.

B. Ineligible properties.

1. Manufactured home parks and group homes (unless the group home is a Section 202 refinance) are not eligible under this Section.
2. Properties whose required repairs are so extensive that they meet the threshold for substantial rehabilitation are not eligible under this Section.

C. Repairs.

1. Critical repairs must be performed prior to endorsement.
2. Non-critical repairs, approved by HUD, may be completed after endorsement with work write-ups sufficiently detailed to facilitate inspections, schedules for completion of repairs, complete bids on work items greater than $25,000, and a financial escrow equal to 120% of the non-critical repair costs that must be established at closing.
3. Fair Housing Act Noncompliance. Any property available for first occupancy after March 13, 1991, that is in noncompliance with Fair Housing Act design and construction requirements must, as a condition of insurance, be modified/ retrofitted to comply with Fair Housing Act accessibility guidelines. HUD may approve the modifications/retrofits to be completed after endorsement with appropriate financial escrows at closing, and the work must be performed in accordance with instructions in Section 3.2. J and Appendix 5C.

D. Elderly developments. Existing projects specifically designed for the elderly, age 62 and over, are eligible under Section 223(f) as long as the property does not contain the features of the Section 232 program described in Section 3.4.S.

E. Prior Defaults/Claims. HUD does not prohibit applications for mortgage insurance for formerly HUD-held loans but will not accept any application from a borrower/principal who has not proven to be a good business partner with HUD or for a property which has proven to be unsuccessful in the past. The Lender should accept such applications only after they have documented the economic, physical, operational or management changes that have occurred which would justify an application for new insurance. A concept meeting prior to submission is required to address the past experience of the loan and of the borrower/principal including past Regulatory Agreement compliance.

F. Labor standards. Davis Bacon prevailing wage requirements do not apply to Section 207/223(f).

G. Prepayment Provisions and Prohibition. The National Housing Act prohibits prepayment of loans insured under Section 223(f) for 5 years from the date of endorsement for insurance except where at the time of prepayment:

1. The borrower enters into an agreement with HUD to maintain the property as rental housing for the remainder of the specified 5 year term;
2. HUD determines that the conversion of the property to a cooperative or condominium ownership is sponsored by a bona fide resident organization representing the majority of households in the project;
3. HUD determines that continuation of the property as rental housing is unnecessary to assure adequate rental housing for low and moderate income residents of the community; or

4. HUD determines that continuation of the property as rental housing would have an undesirable and deleterious effect on the community.

   A Section 223(f) Use Agreement is required for a refinancing of an existing Section 207 insured loan pursuant to Section 223(f)/ 223(a)(7) if the mortgage is aged less than five years from the Final Endorsement date.

H. Eligible Borrowers. Both for-profit and nonprofit borrowers are eligible to apply.

I. Maximum Loan Ratios and DSCR. The following loan ratios and percentages are required to complete the Form HUD-92264-A, Supplement to Project Analysis, mortgage criteria. The lowest of the mortgage criterion controls the loan amount. See Chapter 8, Mortgage Credit Underwriting and Processing Requirements, for more complete form instructions.

Section 223(f)

Refinance and Acquisition Processing

Criteria 1:

Loan Amount Requested on Application. The requested application amount may be amended when appropriate.

Criteria 3:

Amount Based on Value: The applicable percentage of the estimated value of the property after completion of repairs and improvements.

a. 90% - for Section 202 & 202/8 direct loans
b. 87% - for projects with 90% or greater rental assistance
c. 85% - for projects that meet the definition of Affordable Housing ; or
d. 83.3% - for market rate projects

Criteria 4:

Amount Based on Limitations per Family Unit: Where percentages are required, enter the same percentage applied under Criteria 3. See Chapter 8 for complete details and the MF Housing website: http://www.hud.gov/offices/hsg/mfh/hicost/hicost.cfm on information for per family unit limitations and the High Cost Percentage by jurisdiction.

Criteria 5:

Amount Based on DSCR (ratios are rounded for presentation purposes):

a. 90% (1.11 DSCR) - for Section 202 & 202/8 direct loans
b. 87% (1.15 DSCR) - for projects with 90% or greater rental assistance
c. 85% (1.18 DSCR) - for projects that meet the definition of Affordable Housing; or
d. 83.3% (1.20 DSCR) - for market rate projects

Acquisition Applications

Criteria 7:

Amount Based on Total Cost of Acquisition Section 223(f). The following percentages apply to Line 7d. (i.e. formula to compute the loan closing charges) and Line 7h.:

a. 90% - for Section 202 & 202/8 direct loans

b. 87% - for projects with 90% or greater rental assistance

b. 85% - for projects that meet the definition of Affordable Housing ; or

c. 83.3% - for market rate projects

Criteria 10: The greater of 80% of LTV, or the Cost to Refinance.

Criteria 11: See Chapters 8 and 14 for details.

J. Cash Out/Equity Out Proceeds. Fifty percent (50%) of any cash out proceeds after funding mortgagable transaction costs and the assurance of completion requirements must be held in an escrow by the Lender until the required non-critical repairs are completed and HUD approves the release. (See Chapter 8 for detailed escrow release instructions).

K. Reserve for Replacements. Deposits must be made to the Reserve for Replacements. (See Chapter 7 for reserve calculations.)

L. Secondary Financing. HUD permits secondary financing on Section 223(f) loans on affordable housing projects. (See Chapter 8 for details.)

M. Commercial Space. Commercial space is limited to 20% of total net rentable area and commercial income to 20% of effective gross project income.

N. Real Estate Requirements. The mortgage must be on real estate held:

1. In fee simple; or
2. Under a ground lease approved by HUD with a minimum term of 50 years from the date the mortgage is executed.

O. Mortgage Term. The maximum term of the mortgage is 35 years or 75% of the remaining economic life of the property, whichever is less, provided that the term may not be less than 10 years. . (See Section 8.5 and 24 CFR 200.82)

P. Firm Commitment Processing Only. Pre-application is not required for Section 223(f). A concept meeting with the Hub/PC prior to application submission is encouraged if there are concerns about marketability, environment, competing proposals or for projects with significant cash out or large loans.

Q. Physical Occupancy Standards. Section 223(f) has minimum and maximum physical occupancy eligibility and underwriting requirements. See Section 7.6.A.7 for further details.

R. Market Study. Section 223(f) applications typically do not require a market study separate from that contained in the appraisal. However, in volatile or declining markets, the Lender should consider and may be required to obtain a market study to support the underwriting conclusions of

market demand for the property over the loan term. Hub/PC staff should consult with Economic Market Analysis Division (EMAD) in such cases. Requirements for market studies are contained in Chapter 7.

S. Discounts and/or Costs of Issuance associated with bond financing may be eligible for inclusion in the computation of Criteria 7 and 10.

1. Review documentation regarding permanent financing. Documentation must state the amount of the discounts, financing fees, and/or costs of issuance to be charged and with whom they will be paid.
2. Permanent Placement Fee. This fee must include all permanent placement expenses, including Lender's legal fees, except discounts. Where GNMA Mortgage-Backed Securities (MBS) are involved and the mortgagee charges:
   a. The maximum permanent placement fee, it may not assess an additional charge for either the MBS application fee and/or the securities custodial fee.
   b. Less than the maximum permanent placement fee, it may assess an additional charge for either the MBS application fee and/or the securities custodial fee provided the total fees and charges do not exceed the dollar value of the maximum permitted permanent placement fee.
3. Determine if the discounts, financing fees and costs of issuance are reasonable and generally in line with prevailing market conditions and mortgage credit data.

   Recognize financing fees and discounts charged by the permanent Lender, for inclusion in the mortgage:

   a. Bond fees included in the mortgage transaction:
      (1) Where a project is to be financed through the sale of either taxable or tax-exempt bonds, the maximum financing fees allowable in the mortgage computation and recognizable for cost certification purposes is 5.5% of the mortgage amount. Any cost beyond the 5.5% must be paid from sources outside the mortgage.
      (2) The maximum financing fee the mortgagee may retain for its own account is 3.5% to cover the costs of origination, permanent placement, processing, underwriting, closing and delivery (including the mortgagee's legal fees), escrow monitoring, etc. The remaining 2% (or such greater percentage as may result from the Lender reducing its maximum retained 3.5% fee) may be used to offset the bond fees.
   b. Discounts. In a refinancing or purchase transaction, discounts will be recognized only for those actual costs charged by the placement Lender, which are determined to be eligible. Discounts included in the computation of Criteria 7 and 10 must be reasonable based on current market conditions.

3.10 Property Insurance Requirements

A. Insurance During Construction.

1. Public Liability Insurance on a Commercial General Liability form with limits of not less than $500,000 per occurrence to protect the mortgagee during the construction phase from claims involving bodily injury and/or death and damage to the property of others. Such Commercial General Liability Insurance must be endorsed to include owners' and contractors' protective coverage.
2. Vehicle Liability Insurance with limits of not less than $300,000 for one person and $500,000 for more than one person to protect the mortgagee for claims for bodily injury and/or death, and not less than $100,000 against claims for damage to property of others arising from the owner's operation of vehicles. Such insurance must include coverage for employer's owned, non-owned and/or hired vehicles, where applicable.

B. Permanent Insurance

Upon acceptance of the project, or any portion thereof from the contractor, the Lender must provide a certified duplicate copy of the following insurance coverage. In some instances, continuation of the insurance obtained for the construction period, with proper endorsements thereto, will be acceptable. In any event, the Lender must assure that there is no gap period in insurance protection during the transition from the Insurance During Construction to the Permanent Insurance.

1. Public Liability Insurance on a Commercial General Liability form with limits of not less than $500,000 per occurrence to protect the mortgagee from claims involving bodily injury and/or death and property damage which may arise from the mortgagee’s operations, including any use or occupancy of its facilities, grounds and structures, and must include independent contractors coverage, where applicable.
2. Vehicle Liability Insurance. If the mortgagee owns a vehicle in the operation of the project, including non-owned and/or hired vehicles operated for the benefit of the mortgagee, the mortgagee must maintain Vehicle Liability Insurance. Such insurance must provide for limits of liability of not less than $300,000 for one person and $500,000 for more than one person to protect the mortgagee from claims for bodily injury and/or death, and not less than $100,000 against claims for damage to property of others.

C. Other Insurance Requirements

Both HUD and the Lender must be named as additional insured on the policies of insurance.

All insurance carriers or providers which issue policies of insurance on a HUD insured project must have and must maintain during the policy period a rating that is acceptable to HUD.

Chapter 4

Application Processing

4.1 Introduction

A. Only an approved MAP Lender and MAP Underwriter may submit an application for insurance using MAP.

B. Lenders must participate in a concept meeting with the Hub/PC prior to application submission for: a) all market rate and affordable new construction/substantial rehabilitation projects, and b) refinancing/purchase transactions if there are concerns about marketability, environment, competing proposals or for projects with significant cash out or large loans. Market rate new construction and substantial rehabilitation projects require two-stage application processing under which the Lender must submit exhibits for a pre-application review. HUD will decide whether to invite the Lender to submit an application for Firm Commitment. After the Lender submits the required exhibits for the Firm Commitment application, HUD will decide whether to issue a Firm Commitment. HUD technical staff reviews will be documented in the checklists included in the Appendices to this Guide, loan committee review analyses or alternative formats approved by the Hub Director. For affordable projects, the Lender may either process that application with two stages or may combine both stages into the Firm commitment processing phase.

   When a Lender submits an application directly for Firm Commitment for an affordable transaction, they must include all of the exhibits required at pre-application with the exhibits required for Firm Commitment processing, and perform all of the underwriting responsibilities for pre-application and Firm Commitment processing.

C. For acquisition or refinance under Section 223(f), there is no Pre-application stage and the Lender may submit an application for a Firm Commitment.

D. The Site Appraisal and Market Analysis (SAMA) stage and the Conditional Commitment stage are not applicable under MAP.

E. The submission of computerized forms generated by a Lender is acceptable, so long as the recreated form has the Office Management and Budget (OMB) number, expiration date, form title, form number, is identical in content and in the order of the line items on the MAP Form. The recreated form must be completed subject to the instructions included on that form in the MAP Forms Book.

F. Review of MAP Lender Team Members. HUD staff must check the Limited Denial of Participation List and the Consolidated List of Suspended and Debarred Contractors for all proposed Lender team members. The Team Leader will request immediate review by the technical staff of the proposed team members and will advise the Lender within 5 days if the Hub/PC has a concern with a particular reviewer's qualifications or past performance. If a Lender

reviewer who is a concern has prepared the pre-application materials, the Team Leader may halt processing and advise the Lender, or may make substitution of the reviewer a condition of the invitation letter.

4.2 Stages of Application

A. Informal Information

The Hub/PC should respond to informal inquiries, but must not commit HUD to approve a transaction's market acceptability, issue an invitation for an application or for Firm Commitment, or make commitments based on informal discussions or communications. HUD will approve or disapprove an application for insurance in accordance with this Guide. See the following website for a list of the Hub MAP Coordinators: www.hud.gov/offices/hsg/mfh/map/coordinators.cfm.

1. New Project Concept Meeting

Lenders must participate in a concept meeting with the Hub/PC prior to application submission for: a) all market rate and affordable new construction/substantial rehabilitation projects, and b) refinancing/purchase transactions if there are concerns about marketability, environment, competing proposals or for projects with significant cash out or large loans. The Hub MAP Coordinator will schedule the meeting either in person or by teleconference. The submissions from the Lender for a concept meeting review should address the following items, to the extent possible at this stage.

a. Construction/Substantial Rehabilitation Proposals:

- Section of the Act
- Number of market rate and affordable units
- Projected mortgage amount
- Basic information on developer and principals
- Management company
- General contractor
- Previous HUD experience
- Geographic location with map
- Photographs of the subject and immediate surroundings
- Site improvements (existing/proposed)
- Commercial component – discuss potential residents
- Amenities
- Community / city / state support
- Green / sustainability Issues
- Development status (e.g., have any permits/approvals been obtained?)
- Discuss general market conditions, competitive properties and comparables
- Environmental issues
- Potential risks and mitigating factors
- Any anticipated waiver requests

b. Refinance or Acquisition Proposals:

- Section of the Act
- Number of market rate and affordable units
- Projected mortgage amount
- Mortgage term and estimated remaining economic life
- Refinance or acquisition
- Basic information on developer and principals
- Management company
- Previous HUD experience
- Geographic location with map
- Photographs of the subject and immediate surroundings
- Actual and effective property age / class
- Physical condition (a PCNA is not required for the concept meeting)
- Prior / proposed renovations (per unit cost)
- Discuss eligibility for Section 223(f) versus substantial rehabilitation
- Amenities
- Existing debt / cash out
- Current occupancy (physical / economic)
- Income and expenses
- Discuss green / sustainability issues as appropriate
- Discuss general market conditions, competitive properties and comparables
- Environmental issues
- Actual / potential risks and mitigating factors
- Any anticipated waiver requests

The Lender should complete Form HUD-92013, "Application for a Multifamily Housing Project" to the extent possible for the concept meeting.

Where practicable, site visits by the appropriate HUD staff are encouraged. HUD will respond in writing (either by electronic mail or more formally) within 5 business days of the concept meeting/site visit. Consideration should be given to the effect on other insured projects in the subject's market area that are already in the pipeline or in portfolio, developer experience and overall feasibility based on the exhibits and information presented. Depending on the completeness and quality of the submission, HUD may recommend that the Lender submit an application, or may request additional information or specify conditions or recommendations to consider. The written response to the concept meeting must state that it does not represent a commitment from HUD or that a letter of invitation will be issued.

c. Mortgage Credit Pre-Approval of Principals with Large Concentrations of FHA Insured Debt.

The Lender must perform a preliminary but thorough mortgage credit review and obtain HUD approval before submission of the application in cases where principals have greater than $250,000,000 of outstanding FHA insured debt (not including any insured debt under the HFA or GSE risk sharing programs). Based on the Lender's review of the principal's

Schedule of Real Estate Owned, the Lender must identify principals that exceed the $250,000,000 threshold (do not adjust the loan total by the principal's fractional ownership of the real estate). Lenders must obtain HUD pre-approval before such principals or borrowers may apply for additional insurance commitments. The Lender's presentation to the Hub/PC must be approved by National Loan Committee and must address the following items:

1. An analysis of the borrower's financial strength, credit history and experience.
2. An account of FHA and conventional debt on the REO schedule.
3. An explanation of the terms of the principal's existing mortgage debt, e.g. type, maturity, age, interest rate.
4. A full review and analysis of the operating performance and physical condition of the principal's existing FHA insured properties.

NOTE: HUD intends to issue additional guidance and procedures for implementing the requirements of this section.

B. Approval of Lender's Reviewers

The Lender's underwriter for the pre-application or the application for Firm Commitment must be approved by the appropriate Hub/PC before application submission. The Construction Loan Administrator must be approved prior to the Firm Commitment stage. The Lender is responsible for selection and management of their third party consultants and must identify the firms and individuals performing such work when submitting the request for approval of the underwriter. The Hub/PC should review the request and respond within 5-days or the underwriter and the team may presume to be approved. If a Hub/PC has concerns about an underwriter or a proposed third party consultant, they should contact LQMD before responding to the Lender.

C. Pre-application. The pre-application stage for new construction or substantial rehabilitation is designed to permit HUD to review the feasibility of a proposed project. After the review, HUD may invite the Lender to submit an application for a Firm Commitment. No application fee is required for affordable housing pre-applications that submit for two-stage processing and affordable borrowers may pay the required 30 basis point fee with the submission of the Firm Commitment application. Market rate pre-applications must pay a non-refundable 15 basis point review fee, which will be credited to the 30 basis point Firm Commitment fee if an invitation letter is issued and a Firm Commitment application is submitted. The Hub/PC may request additional information if it believes that such information is required for its review.

1. The pre-application appraisal requires a narrative rental and expense analysis with the submission of Forms HUD-92264, 92264-T, if applicable, 92274, and the 92273 and an estimate of land value for new construction projects (or "as is" value for substantial rehabilitation project) by comparable analysis, per the requirements of Chapter 7. The complete appraisal with the appraiser's cost analysis must be submitted with the application for Firm Commitment.

2. The Lender's assessment and preliminary evaluation of the sponsor's and development team's experience and creditworthiness is required with the pre-application. While the full mortgage

credit review is conducted at the Firm Commitment stage, to the extent the borrower entity and principals have been identified at this stage, initial information about the sponsor's experience and a brief summary of mortgage credit qualifications is helpful. The schedule of real estate owned and maturing debt will be provided with the application for Firm Commitment.

D. Letter of Invitation

1. After the pre-application review, the Hub/PC may send a letter to the Lender inviting an application for a Firm Commitment and specifying any conditions or issues to be addressed at the Firm Commitment stage, or may decline to issue an invitation letter.
2. If an invitation letter is issued, the Lender must advise HUD in writing within 30 calendar days if it plans to submit a Firm Commitment application. If it fails to notify HUD, the invitation letter will expire and the Lender will be required to repeat the pre-application process. Letters of invitation are issued and effective for 120 calendar days.
3. The application for a Firm Commitment must be submitted within 120 days of the date of the letter of invitation. The Hub Director may authorize three 30-day extensions (or one 90-day extension) of the 120-day limit, but there is no requirement that the Lender's request for extensions be approved. The Hub Director will review the circumstances reported by the Lender to justify the extension of time and must determine that the requested delay beyond 120 days is not likely to change the underwriting data on which the invitation was based or to undermine the feasibility of the project due to a change in the market or other factors that were previously determined to be acceptable at pre-application.

   If there is a justifiable request by the Lender for an extension of time beyond the 90-days allowed, the Hub Director must request approval for a further extension from the Director of the Office of Multifamily Development, in HQ stating the additional time requested, the Hub Director's recommendation and the reasons for the extension.

E. Firm Commitment Application

1. After receiving an invitation to submit an application for a Firm Commitment, the Lender will complete the application processing based on a full underwriting analysis of the transaction and must present its recommendation in the Narrative Summary. The exhibits that accompany the application are listed in Section 4.3.
2. Applications which the Hub/PC determines to be unacceptable will be returned to the Lender and HUD will retain the application fee. The Hub/PC will advise the Lender of any minor defects or deficiencies in the application and the Lender will have 5 business days to correct the defects or deficiencies. If the defects/deficiencies cannot be corrected within the 5 business days, at such other time frame as the Hub Director determines as appropriate, HUD will reject the application.

F. Due Diligence Requirements for Extension Requests.

The appraisal and the market study (where applicable) must have an effective date within 120-days before the date of the pre-application or the Firm Commitment application and must be updated in accordance with the requirements of Chapter 7.

Hub Directors with the authority to grant additional application processing extensions beyond the timeframes outlined above and in Section 11.2.D, on a case-by-case basis, so long as prolonged extensions of commitments do not occur and any approval is based on updated due diligence. The Hub Director must document that the requested extension or delay will not significantly change the underwriting data on which the invitation or issued commitment was based or undermine the feasibility of the project due to a change in the market or factors affecting cost. Hubs/PCs granting extensions should ensure that the underwriting data on which the application is based is sufficiently current to be deemed valid and reliable. If the information is dated to the point it is unreliable, extensions must be based on updated due diligence.

4.3 Applications Checklist

A. The Guide chapters describe forms and other reports that the Lender must submit, either as part of the Pre-application or as part of the application for a Firm Commitment.

B. The Appendices to this chapter provide exhibit checklists.

C. Lenders must submit to the MAP Coordinator or their designee an original and 1 hard copy of the underwriting file, exhibits and third party reports and must submit an electronic version of these materials on a disc or a removable drive to the HUD processing office. HUD staff will review the application electronically, or may print or make copies of those portions of the application for which paper copies will expedite their review.

1. Appendix 4A

   Sections 220, 221(d)(3), 221(d)(4) and 231, New Construction and Substantial Rehabilitation, Exhibits Required for Pre-Application Review

   Sections 220, 221(d)(3),221(d)(4) and 231, New Construction and Substantial Rehabilitation, Exhibits Required for Application for Firm Commitment

2. Appendix 4B

   Section 223(f) for Refinance or Purchase of Existing Apartments, Exhibits Required for Application for Firm Commitment.

Chapter 5

Architectural Analysis

5.1 Qualifications, Responsibilities, and Approval of Lender's Representative

A. Qualifications

1. Architectural Analysts and Needs Assessors

   a. Architectural Analyst. The Lender must hire a qualified architectural analyst(s) with experience in multifamily construction. The analyst must be knowledgeable and experienced with local building standards and construction methods for the type of project proposed, including the Federal Fair Housing Accessibility Guidelines. The architectural analyst may also serve as the cost estimator if the qualifications are met.

   NOTE: The architectural analyst(s) must be knowledgeable about the Fair Housing Act's design and construction requirements, which apply to "the design and construction of covered multifamily dwellings for first occupancy" after March 13, 1991, and Section 504/ the Uniform Federal Accessibility Standards (UFAS), which establish guidelines for accessibility by disabled persons in Federal and/or federally-funded facilities and may apply if HUD provides financial assistance to a project. The Americans with Disabilities Act may also be applicable, depending on the type of project insured.

   b. Needs Assessor: The Lender shall hire a qualified engineering firm or needs assessor to prepare the Project Capital Needs Assessment (PCNA) for acquisition/ refinance projects, pursuant to Section 223(f) and 223(A)(7). See Appendix 5H for a description of the needs assessor's qualifications and responsibilities.

2. Lender's Architectural Analyst or Needs Assessor: The Lender must be capable of reviewing all building designs submitted and must employ a qualified architectural reviewer, or contract for the services of a qualified reviewer, to review the architectural plans and specifications. The person providing the architectural services should preferably be a registered architect or engineer but must, at a minimum, have a degree in architecture or engineering with three years of experience in their respective field to provide this service.

3. Lender Technical Specialists. Technical specialists such as mechanical, structural, sanitary, site engineers, etc. may be required for review of a particular project. The principal of the technical specialists' firm must be a licensed professional. The architectural analyst is not required to review structural design details and calculations.

B. Responsibilities

The Lender's architectural analyst:

1. Reviews borrower's required architectural services. (See Section 5.2)
2. Determines that the project design complies with the Minimum Property Standards, local codes, the applicable accessibility requirements and HUD design standards. (See Appendix 5)
3. Determines that borrower's Architect (or other persons or organizations providing architectural services) is qualified to provide the design services to the project and administer the construction contract.
4. Reviews borrower's Architect's certification that the project design complies with the Minimum Property Standards, all applicable local codes and ordinances, Fair Housing Act accessibility requirements and HUD standards. (See Appendix 5C)
5. Determines that the borrower's Architect's liability insurance will be maintained up through the 12-month warranty inspection period that follows Final Endorsement.

C. HUD Approval of Lender's Architectural Analyst and Needs Assessor. The Hub/PC must examine the credentials of all architectural analysts and needs assessors hired by the Lender, and may reject any individuals or firms that it considers unqualified.

5.2 Required Architectural Services for Design and Supervision

The borrower must engage a licensed professional for the design of elevator and walkup projects, projects of 20 or more living units and smaller projects which, in the Hub/PC's judgment are of complex design or construction.

A. Licensing and Insurance. Design and construction professionals must be licensed and must carry liability insurance.

1. Professional License. Architects, engineers and/or designers providing required design and/or construction services must be professionally licensed to render services in the design of buildings by the State in which the project is to be constructed.
2. Professional Liability Insurance.
   a. The Design Architect, the Architect administering the construction contract, and all engineers and/or designers providing required design and/or construction services must each be covered by a policy of professional liability insurance in an amount consistent with insurance industry practice.
   b. The professional liability insurance policy must be maintained up through acceptance of the 12-month warranty inspection period that follows Final Endorsement. The professional liability insurance carrier must have and must maintain a rating that is acceptable to HUD.

c. At initial closing, each Architect and other design and/or construction professional must provide their certificate of liability insurance which must substantially conform to the sample Certificate of Professional Liability Insurance contained in Appendix 5I.1

B. Evaluation and Selection of Architect. HUD, the borrower and the lender must determine that the Project Architect is capable and qualified.

1. The Lender's architectural analyst
   a. Will review the Architect's work progress and product(s);
   b. May recommend that the borrower select another professional if the Architect's work progress or work product(s) is found to be unacceptable.
2. Failure of the borrower to engage an Architect acceptable to the Lender and HUD is a basis for rejection of the application.

C. Owner-Architect Agreement. On projects requiring licensed professional services, an agreement between the Architect and the owner for architectural services must be executed.

1. The owner must submit the agreement with the application for Firm Commitment.
2. The executed agreement must be an AIA Document B108, Standard Form of Agreement between Owner and Architect for Housing Services and must include the HUD Amendment for Federally Funded or Federally Insured Projects.
   a. The scope of services shall provide all architectural, structural, mechanical, electrical, civil, landscape and interior design and consulting services necessary to prepare drawings, specifications and other documents setting forth in detail the requirements for construction of the project. The scope of services shall also provide for administration of the construction contract.
   b. The scope of services must designate the responsibility for the services to be provided, whether by the Architect, owner or others.
   c. Additional Owner-Architect Agreements must be submitted for any part of the basic design services with more than one prime professional, e.g. for site, civil, mechanical, electrical engineering services, etc., or supervisory architectural services. The borrower's Architect is responsible for coordinating multiple prime professional contracts.
3. There may be separate agreements for design and construction services if the same Architect is not employed for each. When there is a separate agreement for administration of the construction contract, it must be submitted for approval before initial endorsement. Where separate agreements are made, those sections not applicable shall be struck out.
4. An Architect with an identity of interest with the owner or general contractor can serve as the Design Architect, but cannot administer the construction contract. An identity of interest is defined in the HUD Amendment.

D. Modification of Owner-Architect Agreement. The document may be changed to reflect the actual agreement between owner and Architect for the specific project.

1. Generally modifications can be made by striking out inapplicable provisions and inserting additional provisions in Article 12. Adding directly to a specific provision is also acceptable.
2. Changes shall not delete any service, either by the Architect or owner, necessary to the project, although the responsibility for a required service may be transferred.
   a. The document shall provide a clear and definite statement of how responsibility for providing any required service is to be divided between Architect, owner and others. Documents must conform to requirements in Section 5.2.C.2 above.
   b. Required services may not be sublet or delegated to any one not identified to or approved by HUD.
3. The Architect's fee must be a fixed fee for the services provided by the Architect as stated in the Agreement. No other method of stating compensation is acceptable. Separate fee amounts for design services and for construction services must be stated.
4. Where the Architect's basic fee exceeds that which may be paid from mortgage proceeds or where the Owner-Architect Agreement provides for reimbursable expenses (note that reimbursable expenses may not be paid from mortgage proceeds), the person/entity responsible for such extra fees must be identified on the HUD Amendment.
5. HUD shall not be incorporated into any specific provision of the Agreement and the inclusion of the HUD Amendment in Article 12 is sufficient to incorporate HUD requirements. No modification of the HUD Amendment is permitted.
6. The Lender's architectural analyst must review the agreement for compliance with these instructions.

E. Architectural Considerations in Industrialized Housing. The Lender's analyst must contact the Hub/PC Director to approve the use of industrialized housing. Architectural and engineering services are also involved in the development of industrialized housing and the fees for such services must be included in the cost of each manufactured unit. The Lender's analysis must determine the acceptability of such services by examining the drawings and specifications.

   a. The exhibits shall be equal in quality to the typical construction documents prepared by Architects engaged in designing the type of housing proposed and should include the working drawings and specifications for the typical industrialized housing unit, along with an assembly plan and proper manufacturer's warranty document.
   b. Additional professional services may be required to provide a complete set of construction documents which must be determined by the Lender's architectural analyst for each project based on how much of the total project is provided by the housing manufacturer. Usually, the architect will integrate the manufacturer's drawings into his/her set of drawings and specifications, adapting them to the particular project.
   c. The manufacturer shall provide complete professional design services. If the services meet in all respects the qualifications and quality required, the construction documents shall be acceptable.

d. Owner-Architect Agreement, AIA Document B108, is required only to cover the services provided by the Architect and is not required for professional services provided by the housing manufacturer.

e. In all cases, an independent Architect with no identity of interest shall provide general administration of the construction contract.

5.3 Architectural Standards and Other Criteria

Projects that are built, substantially rehabilitated or re-financed with FHA mortgage insurance must meet the standards in the Appendices to this chapter, as outlined below:

A. Appendix 5A - Standards for the 220, 221(d), and 231 programs and limited application to the 223(f) program

B. Appendix 5B – Additional standards for 220, 221(d), and 231 programs for substantial rehabilitation

C. Appendix 5C – Additional standards and criteria for the 223(f) program

D. Appendix 5D – Seismic resistance and fire protection standards for substantial rehabilitation and 223(f) programs

E. Appendix 5E – Requirements for firm commitment drawings and specifications for new construction projects

5.4 Architectural Processing – New Construction

A. Lender's Architectural Analyst's Duties

1. Review the borrower's Architectural/Engineering exhibits (Appendix 5E) for compliance with local code and HUD requirements.

   a. Drawings and specifications must be complete and correct.

   b. Acceptable evidence must be provided that the project has or will have necessary utility services and pedestrian and vehicular access.

      (1) Adequate assurance of continuing service by local utility companies and/or local public authorities, or

      (2) Construction documents and contract for completion by borrower's contractor.

2. Visit the site and prepare a written report on physical aspects of on-site and offsite features.

   a. Observe physical features such as existing construction, topography, soil conditions, drainage, vegetation, etc.

   b. Include unusual site conditions and necessary demolition and offsite construction.

c. Determine and comment on HUD environmental conditions and criteria which may affect the proposal.

3. Provide for continuous architectural liaison with the borrower's Architect.
4. Maintain a processing record of all architectural/engineering actions when the proposal is first assigned, including:
   a. File all forms, reports, decisions, and documents relevant to architectural actions in chronological order.
   b. Record all architectural actions, counteractions by others, or actions that may affect design or construction.
   c. Record the receipt of forms and documents, the issuance of letters and memoranda, the completion of forms and worksheets, contacts with the Architect, etc.
   d. Log and briefly describe contacts, including telephone calls, with the Architect.
   e. Keep a journal of architectural actions, including:
      (1) Application for Firm Commitment, Form HUD-92013.
      (2) Reports of site visit (including technical specialists' if made).
      (3) Drawings and specifications identified and dated (if filed elsewhere, reference in journal).
      (4) Owner-Architect Agreement, including HUD Amendment (see Forms Appendix)
      (5) Data used to process (if filed elsewhere, reference in journal).
      (6) Liaison meetings and telephone calls with Architect (include remarks in journal or notes).
      (7) Letters, memoranda, notes and worksheets.
      (8) Soil borings report or other soil exploration data.
      (9) Invitation Letter.
      (10) Form HUD-92264 with any memorandum for Firm Commitment.
      (11) Firm Commitment approval.
      (12) Surveyor's Report, Form HUD-92457M (Initial Endorsement).
5. Guide and assist the borrower's Architect during design development to expedite orderly processing and avoid delays.
   a. Assure that the Architect is licensed to practice within the State where the project is to be constructed.
   b. Assure that the Architect and the borrower execute AIA Document B108, including HUD Amendment.
   c. Provide the Architect a copy of the MAP Guide, applicable HUD program Handbook(s), HUD Minimum Property Standards (MPS) (Handbook 4910.1), and other applicable guides and publications, including reference material for all applicable accessibility laws, especially the Fair Housing Act Design Manual.

d. Discuss with the Architect:
   (1) Lender procedures;
   (2) HUD procedures; and
   (3) Architect's responsibilities.

e. Discuss with the Architect any available housing design data and all HUD-developed or industry norms that are applicable and beneficial to the project.

f. Review the drawings and specifications during design development and identify early any questionable design concepts, elements or deficiencies to avoid costly revisions at advanced stages of exhibit development. Special attention should be paid to accessibility for persons with disabilities. Because no accessibility review is done at Pre-Application stage, it is entirely the responsibility of the Architect to produce a building and site design at Firm Commitment stage that fully conforms to all applicable accessibility laws.

6. Request assistance by the Technical Specialist, e.g., engineers, when necessary.
   a. Review and use the Technical Specialist's Report.
   b. Furnish the Architect with consolidated design requirements, including recommendations or requirements of Technical Specialists.
7. Work with Lender's cost analyst to assure that project cost will fall within the established budget:
   a. Supply cost analyst with a current Davis Bacon wage rate schedule. The HUD Office will include, as part of its Firm Commitment invitation letter, the current Davis Bacon wage rate schedule applicable to the proposed project. **Lender processing staff must keep in contact with HUD labor relations staff to obtain any updates (modifications) to the Davis Bacon wage rate schedule before the Lender submits the Firm Commitment application to HUD**. Once the Firm Commitment application is submitted, HUD labor relations staff will provide any Davis Bacon modifications which may be published and applicable to the construction of the project.
   b. Evaluate appropriateness of type of structure, construction methods and materials considering initial costs and future maintenance.
   c. Prepare or review reserve-for-replacement analysis for completeness of the short-lived item list where the reserve-for-replacement formula has been waived.
8. Report any deviations from accepted concepts or HUD requirements which cannot be resolved with the borrower's Architect by the Lender's underwriter.
9. Be aware of design development progress in relation to established target dates and inform the Lender's underwriter of possible or actual delays or problems.
10. Review architectural/engineering exhibits submitted with the Firm Commitment application.
    a. Assure exhibits are as agreed to during design development, meet conditions of the previous stage, and comply with all HUD standards and criteria.
    b. Prepare the architectural/engineering portions of Form HUD-92264, Rental Housing

Project Income Analysis and Appraisal (See MAP Forms Book), upon completion of architectural analysis.

11. Furnish information to the Lender's cost analyst on the scope of the Architect's work to serve as the basis for estimating the Architect's fee.
12. Assure that drawings and specifications are complete prior to submission of a Firm Commitment application.
13. Review experience and qualifications of general contractor.
14. Prior to initial endorsement:
    a. Review contractor's Progress Schedule.
    b. Review the legal survey and Surveyor's Report/ Certificate.
    c. Assure that HUD's sets of drawings and specifications are sealed and signed.
15. Consult with Technical Specialists. While the Lender's architectural analyst should report obvious errors or omissions to the borrower's Architect, the analyst is not required to review and is not responsible for, the accuracy of structural dimensions or other details that would require a professional structural review. When engineering review, advice and guidance on specific projects or problems is required, the Lender's architectural analyst should request the services of the appropriate engineers (such as mechanical, structural, sanitary, site, etc.).
16. Negotiations.
    a. The Lender's architectural analyst provides guidance to the borrower's Architect and should request the assistance of the borrower if the Architect is reluctant to follow such guidance, however:
        (1) Suggestions for improvement or betterments should not be pursued if they are unacceptable to the borrower.
        (2) HUD mandatory standards and criteria may not be modified or waived.
    b. Report to the Lender's underwriter when resolution is not possible.
        (1) Recommend rejection only if the design fails to comply with prescribed requirements, laws, ordinances or restrictions, or is inadequate in some major respect.
        (2) Request HUD intervention and assistance, describing the deficiency or inadequacy that the Architect and/or sponsor are unwilling or unable to correct.

B. Borrower's Architect's Duties

1. Services. Provides architectural and engineering services in accordance with the Owner-Architect Agreement, including:
    a. Develops documents that conform to the concept of the sponsor's proposal.
    b. Produces drawings and specifications that comply with local requirements and HUD standards and criteria.

2. Data. The Architect's work is shaped by data such as codes, transportation, parking, space and mechanical requirements, which the Architect develops through surveys and research.
3. Lender Assistance. There must be continuous consultation between the borrower's Architect and the Lender's architectural analyst.
4. Pre-application stage. The Architect must:
   a. Visit the site.
   b. Evaluate the borrower's and user's needs.
   c. Become familiar with applicable local and HUD codes, restrictions and requirements.
   d. Develop preliminary sketches.
5. Firm Commitment Stage. Based on the preliminary sketches, the borrower's design Architect must:
   a. Prepare final construction documents after the basic exhibits are approved. These include contract drawings and specifications with:
      (1) Current wage decision,
      (2) Current edition of AIA Document A201, General Conditions of the Contract for Construction, and
      (3) Form HUD-92554M, Supplementary Conditions of the Contract for Construction**.**
   b. Submit the final construction documents to the borrower, to the Lender and to HUD for approval.
6. Construction documents must be complete and:
   a. Clearly define the scope of work.
   b. Define and describe the materials to be used.
   c. Illustrate the construction and methods of assembly.
   d. Contain all necessary information for bidding (if applicable) and constructing the project.
7. Alternates. The Architect may include alternate materials if they are of equal quality, safety and performance, and within the budget. Alternate materials must be selected before a Firm Commitment is issued and should be coordinated with the general contractor so as not to delay the bidding.

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.5 Architectural/Engineering Exhibits – New Construction

A. Pre-application stage for HUD review. The Lender must submit the following Pre-application exhibits to HUD:
   1. Form HUD-92013, Application for Project Mortgage Insurance

2. Location map with property clearly defined.
3. Sketch plan of the site showing overall dimensions of main building(s), major site elements, (e.g. parking lots) and location of existing utilities, (e.g. water, sewer, electric, gas) in the streets adjacent to the site. Contour lines and elevations are not required in the sketch site plan.
4. Sketch plans of main building(s) that show overall dimensions of:
   a. Typical floor plans showing apartment types and placement;
   b. Ground floor plans showing common areas;
   c. Sketch floor plans of typical dwelling units;
   d. Typical wall sections showing footing, foundation, and wall and floor structure. Notes must indicate the basic materials to be used in the structure, floor and exterior finish.

   Sketch plan dimensions must be sufficiently detailed to allow the HUD architectural analyst to calculate the Gross Floor Area for the entire project and the Net Rentable Areas for all the apartment units in the project.

B. Firm Commitment Stage. The borrower must submit the following exhibits for review and comment by the Lender's architectural analyst in the report:

1. Form HUD-92013, Application for Project Mortgage Insurance.
2. Owner-Architect Agreement, AIA Document B108 (and HUD Amendment to the B108, where required), fully defining the services and fees for each prime professional with which the borrower/owner contracts directly. Additional contracts must be submitted for any part of the basic design services with more than one prime professional, e.g. for site, civil, mechanical, electrical engineering services, etc., or supervisory architectural services. The borrower's Architect shall have the authority to coordinate multiple prime professional contracts.
3. Legal Survey. Note that the survey does not have to be new. An existing survey marked "Re-surveyed" and dated within the submission time frame is acceptable, provided that it is either done by the original surveyor or, if performed by a different surveyor, it must also contain the seal of the new licensed surveyor.
4. Completed Surveyor's Report, Form HUD-92457M, with responses to all questions;

   NOTE: The American Land Title Association/American Congress on Surveying and Mapping (ALTA/ACSM) has its own mandatory certification language that differs in wording from HUD's mandatory certification language on Form HUD-92457M. HUD will permit the required ALTA/ACSM certification to appear on the survey map/plat along with the required HUD certification.
5. Engineering and specialty reports, e.g. geotechnical, environmental, noise, flood hazard, toxic hazard, termite control, structural integrity (for Existing or Substantial Rehabilitation projects), heat gain/loss calculations, etc.
6. Municipal and utility company letters of confirmation for the provision of services and/or offsite improvements.

7. Any documents necessary to establish:
   a. Site ingress and egress, utilities service and other general acceptability criteria in MPS 4910.1, Chapter 2.
   b. Binding maintenance agreements where common use easements (e.g. driveways) are present.
8. Certifications from borrower's Architect that:
   a. Foundation designs reflect site soils limitations and design recommendations included in the foundation soils report and any other geotechnical reports (which may be submitted by the soils engineer);
   b. All project structures, amenities, and site improvements are in full compliance with all applicable accessibility laws.
9. Description of any identity of interest that exists between the prime professional providing supervisory architectural services, the owner and the general contractor.
10. Contract drawings and specifications (see Appendix 5E).
11. Offsite Construction: Describe all work outside the boundaries of the property essential to the project (see Appendix 5E).

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.6 Lender Deliverables – New Construction

A. Pre-application Stage for HUD review includes the borrower's architectural/engineering exhibits (see Section 5.5.A).

B. Firm Stage.
   1. Borrower's Architectural/Engineering exhibits for Firm Stage (see Section 5.5B and Appendix 5E);
   2. Review Report prepared by Lender's architectural analyst who must state that all exhibits are acceptable without conditions, and that all deficiencies have been acceptably corrected. The report should address the following:
      a. Completeness of contract documents;
      b. Conformance to local building codes and HUD standards;
      c. Accessibility for persons with disabilities (also refer to the Fair Housing Act design and construction requirements for accessibility found at 42 U.S.C. § 3604(f)(3)(C)(i)-(iii)):
         (1) From property line to main entrance(s) to main building(s);
         (2) To all areas throughout the project site;
         (3) Within all residential structures:
            (a) Path of travel to all public areas;

(b) Path of travel to all dwelling units required to be accessible under applicable accessibility laws;

(c) Within accessible dwelling units, full accessibility to all areas within, and full usability of all areas, including kitchens and bathrooms.

d. Site design:

(1) Placement of buildings, roads, walks and parking on the site;

(2) Site erosion and drainage;

(3) Soil borings report.

e. Building design:

(1) Building circulation:

(a) Adequacy of elevators;

(b) Number and placement of stairs;

(c) Adequacy of lobbies and corridors;

(d) Adequacy of fire egress.

(2) Typical dwelling units: Adequacy of room sizes and circulation within units.

(3) Fire safety: Provision of adequate fire safety measures, e.g. fire sprinklers, firewalls, fire doors (if required).

(4) Structural adequacy: Review of building structure and structural details.

(5) Mechanical and electrical adequacy: Review of mechanical and electrical plans.

(6) Energy efficiency. Review utility combination for energy efficiency and determine acceptability of utility combination. If HUD has required a life cycle utility analysis to be included in the Firm Commitment application, (see Section 5.8.B.1.b) review the utility analysis to determine acceptability of the utility combination. See Appendix 5A, Paragraph O for energy efficiency standards.

f. Review exhibits (see Section 5.5B), and any information relevant to an underwriting decision generated by the duties in Section 5.4A and the responsibilities in Section 5.1B.

g. Prepare or review a reserve-for-replacement analysis in conjunction with the cost analyst where the formula has been waived.

3. Prepare the architectural portion on Form HUD-92264, signed by the Lender's architectural analyst under "Architectural Processor". When the project consists of more than one structure, the Lender must submit an itemized Gross Floor Area and Dwelling Unit Breakdown list, including unit count and unit areas, for each individual structure in the project.

4. Submit copies of the Lender's architectural analyst's project files and logs only if requested by the HUD Office.
5. Standard certification by Lender's architectural analyst (see Chapter 11 Section 11.2).

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.7 Firm Commitment through Initial Endorsement – New Construction

A. Changes after Firm Commitment. Prior to initial endorsement:

1. Drawings and specifications may be amended by addendum when the change(s) will have no effect on cost or value. The Lender's analyst must review the addenda for acceptability.
   a. Addenda must clearly state or show the change with specific reference to the location of the item on the drawings or in the specifications.
   b. Amendments shall be clearly noted and dated.
   c. Addenda are not to be used to correct errors noted during Firm Commitment processing.
2. Firm Commitment reprocessing is required for major changes adding or deleting work, or affecting cost or value. Drawings and specifications affected must have sheets and pages revised and replaced.

B. Contractor's Estimated Progress Schedule. Article 3.10.1 of the AIA General Conditions requires the general contractor to prepare and submit an "estimated progress schedule for the work" to the borrower and Architect.

1. The borrower or Architect must submit a copy to the Lender's analyst at least 30 days before Initial Endorsement.
2. The Lender's analyst must review the schedule to assure it relates to the entire project to the extent required by the contract documents, inclusive of dates for the stages of construction.

   Copies of the approved schedule are given to the HUD Inspector to determine scheduled progress at each site visit.
3. The Lender must use the schedule to determine when construction is falling behind, triggering a meeting of all parties to the contract, including the bonding company. The meeting is to determine the reason for delays, advise of the consequences of the delay and develop a plan to get construction back on schedule.

C. Contract Documents. The Lender shall submit the following contract documents to HUD's architectural staff for review and approval prior to Initial Endorsement:

1. Building Loan Agreement, Form HUD-92441M, and Construction Contract, Form HUD-92442M.

a. Correct identification of drawings and specifications on forms.

(1) Project name, HUD project number, and design Architect's name.

(2) Drawings and specifications by sheets, pages and date or by index with date of last revision of sheet and page.

(3) Addendum by number and date.

b. Compliance with any architectural requirement or condition.

2. Survey and Surveyor's Report, Form HUD-92457M, must be reviewed:

a. For compliance with Survey Instructions and Certificate.

b. To confirm that legal description and survey property boundaries agree.

c. To assure that the surveyor's report is complete per instructions.

3. Drawings and Specifications. Submit three sets and confirm that:

a. Master Sets No. 1, 2 and 3 are the same as accepted and identified in the Firm Commitment. Indicate the total number of pages in the drawings and specifications. Hub/PCs may, at their discretion, eliminate the requirement for set No. 2 (Hub/PC review set).

b. Cover and last drawing sheets, and the first and last specification pages of all sets, must be signed by representatives of the design Architect, Architect administering contract, owner, contractor, Lender and bonding company, if any.

c. Master Set must be bound and signed as described above on the cover sheet and last sheet of the drawings and the first and last pages of the specifications. Signatories must initial opposite any "last minute" revisions not covered by Firm Commitment or addendum. The master set must be identified as such.

d. Lender signatory:

The Lender must have an individual or individuals who are authorized to sign at closing, and who must sign and initial the plans and specifications (Appendix 5E). HUD will only accept the Lender's authorized signatory, who must be identified as such for HUD by the Lender.

4. Drawings and Specifications. Lender must retain one set and confirm that the:

b. Lender set is the same as the set that was accepted and identified in the Firm commitment. Indicate the total number of pages in the drawings and specifications.

c. Cover sheets are signed by representatives of the design Architect, Architect administering contract, owner, contractor, Lender and bonding company, if any.

d. Lender set is signed by signatories on the cover sheet and the last sheet of the drawings and the first and last pages of the specifications. Signatories must initial opposite any "last minute" revisions not covered by Firm Commitment or addendum.

D. If contract documents are correct, the HUD Team Leader will recommend Initial Endorsement. In the event of errors or inconsistencies, the contract documents will be returned to the Lender for correction and resubmission.

E. Distribution of Drawings and Specifications.

1. After Initial Endorsement, HUD will distribute the drawings and specifications as follows:
   a. Set No. 1, Master Set, is the legal contract document. HUD will:
      (1) Retain this set until the last guarantee inspection.
         (a) Add a copy of each Change Order, Form HUD-92437.
         (b) Add a copy of each Architect's Supplemental Instruction.
      (2) Package the specifications in a tightly rolled bundle with drawings on the outside, attach a memo indicating the HUD project number, and send it to the Regional Federal Records Center 1 year after completion of construction.
   b. Set No. 2 is the HUD Office's review set.
      (1) HUD staff will use this set for processing change orders, review of inspections and similar functions.
      (2) Dispose of this set after Final Endorsement.
   c. Set No. 3 is the HUD Office's job site set.
      (1) The HUD Inspector will use this set for inspection of the project.
      (2) The HUD Inspector will conform this set to the contractor's "record set." (The Contractor is required to maintain at the site a record set for the Owner.)
      (3) HUD Inspector will return this set to the HUD Office upon completion of construction. This set is the HUD "as-built" set.
      (4) Use this set for guarantee inspections.
      (5) Send the "as-built" set to the Hub Director, 1 year after completion of construction, for use in loan servicing.
2. Drawings and specifications to be maintained by the Lender (the Lender set):
   a. The Lender must maintain this set for a period of 3 years after Final Endorsement.
      (1) Add a copy of each Change Order, Form HUD-92437.
      (2) Add a copy of each Architect's Supplemental Instruction.
   b. If the originating Lender will not administer the construction contract, the Construction Administrating Lender must forward copies of each Change Order and Architect's Supplemental Instruction to the originating Lender for inclusion in the Lender Set.

F. Early Start of Construction. Construction may not start before initial endorsement and recordation of the insured mortgage, except with the prior approval of the Hub Director. Any work performed after receipt by HUD of the initial application, including clearing, grading or other preliminary work, constitutes the early start of construction.

The following are mandatory conditions for approval of an early start of construction:

1. Firm Commitment. There must be a valid outstanding Firm Commitment, including:
   a. Site control, and the right to legally access the site for purposes of construction.
   b. HUD-approved set of contract drawings and specifications on file. See Appendix 5I for required Firm Commitment contract drawings and specifications.
   c. Required construction contract and other construction documents, including, but not limited to:
      (1) Construction Contract, Form HUD-92442M;
      (2) Supplementary Conditions of the Contract for Construction, Form HUD-92554M;
      (3) Applicable Davis-Bacon wage decision (supplied by HUD Labor Relations);
2. Assurance of Completion for On-Site and Off-Site work. The early start may not hamper the ability to obtain a title policy when the loan goes to initial closing.
3. Valid Basis for Early Start. The Hub Director must document the file including the reason for granting an early start, after determining that:
   a. An immediate closing is not practical.
   b. There is reasonable evidence and assurance that closing will occur in the near future.
   c. There is a compelling need to start construction before the anticipated closing date.
   d. An early start of construction will not be detrimental to HUD's interests.
   e. HUD has no insurance obligation or liability whatsoever for costs incurred during an early start if the project does not reach endorsement.
4. The contractor, borrower and Lender must execute Form HUD-92415, Request for Permission to Commence Construction Prior to Initial Endorsement for Mortgage Insurance, without change. The Hub/PC Director must sign Form HUD-92415.
5. Preconstruction conference must be held before the start of any construction (see Chapter 13 Section 13.2).
6. Violations of Early Start Criteria must be referred to the Hub Director for a determination as to whether the project may proceed to Initial Endorsement.

5.8 HUD Procedures - Pre-Application Stage – New Construction

A. The Lender must submit Pre-application deliverables (Section 5.6) to the Hub/PC.

B. The HUD architectural analyst will examine the Architectural/Engineering (A/E) exhibits and will recommend either acceptance or rejection of the A/E portion of the Pre-application submission. Using the application and the sketch plans, the HUD architectural analyst will review the pre-application submission and report to the MAP Team Leader using the form at Appendix 5F.

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.9 HUD Procedures: Firm Stage – New Construction

A. The Lender must submit the firm deliverables (Section 5.6) to the Hub/PC. The HUD architectural analyst will examine the Lender's review, the underwriting summary and the A/E exhibits and will review the quality of the Lender's review and the transaction itself. The HUD analyst will not reprocess the case. However, if the HUD analyst determines that certain underwriting conclusions are not supportable and affect HUD's risk, the analyst may recommend that the Lender modify the application or may recommend a rejection. The Team Leader will approve, reject or modify the recommendation of the HUD Architectural analyst.

B. The HUD architectural analyst will:

1. Review the Firm Commitment deliverables for completeness;
2. Examine the review report and the A/E exhibits and will recommend either acceptance or rejection of the A/E portion of the Firm Commitment submission and will report to the Team Leader on the form at Appendix 5F.1. HUD A/E recommendations will be based on areas of concern in the review report not covered at Pre-application stage.

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.10 HUD Procedures - Firm Commitment through Initial Endorsement – New Construction

A. HUD architectural staff will review contract documents as indicated in Section 5.7.C prior to Initial Endorsement.

B. If the contract documents are correct, the Team Leader will recommend Initial Endorsement. In the event of errors or inconsistencies, the contract documents will be returned to the Lender for correction and resubmission.

C. The contract drawings and specifications will be distributed as indicated in Section 5.7.E.

5.11 General Lender Procedures – Substantial Rehabilitation

All of the previous instructions in this Chapter apply to substantial rehabilitation projects unless otherwise modified therein.

5.12 Definitions – Substantial Rehabilitation

A. Substantial Rehabilitation - required repairs, replacements and improvements involve:

1. The replacement of two or more major building components, or
2. Costs which exceed the greater of:
   a. 15% (exclusive of any soft costs) of the property's replacement cost (fair market value) after completion of all required repairs, replacements, and improvements,
   b. $6,500 per dwelling unit (adjusted by HUD's authorized high cost percentage), or
   c. 20% of the mortgage proceeds applied to rehabilitation expenses.

   NOTE: Estimates for determining the cost for substantial rehabilitation must include general requirements and fees for contractor's general overhead and profit, bond premium, borrower's and contractor's other fees and design architect and supervisory architect. However, when determining the eligibility of Section 223(f) projects, include only the direct repair costs and do not add general requirements and fees.

B. Major Building Component. Roof structures, wall or floor structures, foundations, plumbing, central heating and air conditioning systems, or electrical systems.

1. Major component refers to the importance of the component and the extent of replacement.
   a. The component must be significant to the building and its use and normally be expected to last the useful life of the structure, and not be minor or cosmetic. Examples of major components: roof sheathing, rafters, framing members. Examples of minor components: shingles, built-up-roofing.
   b. Total replacement of major components is not required, but at least 50% of the component must be replaced.

5.13 Standards – Substantial Rehabilitation

Substantial rehabilitation must comply with applicable local codes and ordinances. For a full listing of standards and guidelines for substantial rehabilitation projects, see Appendix 5B and 5D.

5.14 Architectural/Engineering Exhibits – Substantial Rehabilitation - Firm Stage

In addition to the exhibits indicated in Section 5.5, the borrower shall submit the following exhibits for the Lender's architectural analyst to review:

A. Detailed scope of rehabilitation work resulting from joint inspection (see Section 5.16).

B. If an unusual amount of time has elapsed since the joint inspection, or if property damage may have occurred, re-inspect the property to determine the current physical condition and provide any necessary additional conditions for the Firm Commitment.

5.15 Lender Deliverables – Substantial Rehabilitation

In addition to the deliverables in Section 5.6, the Lender must present the following deliverables to Hub/PC:

A. Pre-application stage:

1. Sketch plans of the existing building(s) "as-is".
2. Basic Work Write-up: Description of the proposed rehabilitation (from preliminary inspection of the property conducted by borrower's Architect), including post-rehabilitation sketch plans. This precedes the joint inspection and the Detailed Work Write-up (see Sections 5.16 and 5.17).
3. Lead Based Paint (LBP) and asbestos test reports for projects constructed prior to 1978 (see LBP and asbestos standards in Appendix 5B, paragraph H, and Chapter 9 Sections 9.4.D and 9.7.B.).

B. Firm Commitment Stage:

1. Borrower's Architectural/Engineering exhibits for substantial rehabilitation (see Section 5.14).
2. Review Report prepared by Lender's architectural analyst covering the Scope of Rehabilitation Work (Section 5.16) and the Detail Work Write-up (Section 5.17). Where the project qualifies as substantial rehabilitation, the report must address each component and how it meets the "major building component" definition.
3. Area and unit count breakdowns for multiple structure projects:

   For projects containing multiple structures, provide an individual breakdown of gross floor area, net rentable area and dwelling unit distribution (including net area and number of each unit type) for each typical building design.
4. Prepared architectural portion on Form HUD-92264, signed by Lender's architectural analyst under "Architectural Processor." When the project consists of more than one structure, the Lender must submit an itemized Gross Floor Area and Dwelling Unit Breakdown list, including unit count and unit areas, for each individual structure in the project.
5. Copies of Lender's architectural analyst's project files and logs but only at the request of the Hub/PC.
6. Standard certification by Lender's architectural analyst (see Chapter 11 Section 11.2).

7. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.16 Joint Inspection – Substantial Rehabilitation

As soon as possible after the pre-application approval is issued by HUD, the Lender should schedule an on-site inspection with the borrower.

A. In-Site Inspection Participants:
   1. Architectural and cost staff employed by the Lender, the borrower's Architect, and the general contractor must attend the on-site inspection. A representative of the local building department should be present and if they are not, the team must have a copy of the latest official inspection for compliance with local codes and ordinances.

B. Purpose.
   1. Determine the property condition, particularly concerning major defects, deterioration and obsolescence.
   2. Determine type and extent of work that would:
      a. Appropriately rehabilitate the property for the intended occupants.
      b. Result in reasonable operating costs.
      c. Ensure continued marketability after rehabilitation.

C. Scope. Since the joint inspection is the basis for the detailed work write-up, cost estimate, commitment conditions and required exhibits, the inspection must be thorough and include:
   1. All features of the project site; buildings and improvements, utilities, roads and parking, underground storage tanks and surroundings.
   2. Sufficient living units to ascertain all necessary rehabilitation. This may range from selected typical units to all the units, depending on physical conditions.

5.17 Detailed Work Write-up – Substantial Rehabilitation

The borrower's Architect will prepare the detailed work write-up reflecting the agreed work, based on the joint inspection. Or, the borrower's Architect may bypass the detailed work write-up stage and proceed directly to preparation of drawings and specifications that clearly describe the work agreed to, in lieu of a work write-up. (Bypassing the work write-up stage must be approved by the Lender's architectural analyst.) Because there is no initial deposit to the Reserve for Replacements for substantial rehabilitation, the scope of work must provide for the replacement of all doors, windows roofs, cabinets, and mechanical/conveyance systems (e.g. elevators, plumbing, boilers/furnaces, ventilation/air conditioning,

electrical) which are at or near the end of their useful lives and must result in a structure which will require no complete replacement of doors, windows, roofs, cabinets, or mechanical/conveyance systems for at least 5 years.

A. The detailed work write-up must describe in narrative form the required rehabilitation, general requirements and special requirements.

   1. General Requirements.

      a. Include work items applicable to all elements in the project, for example: site work, exterior work, painting and decorating, rehabilitation of kitchens, bathrooms, roofs, mechanical systems, electrical systems, interior walls, floors, windows and doors, etc.

      b. For projects that contain LBP and/or asbestos:

         (1) The borrower or its Architect is responsible for engaging the services of a qualified LBP and/or asbestos abatement contractor(s) to prepare a scope of work for the abatement. Where the scope of abatement work consists of permanent enclosure or encapsulation, but not removal, the qualified abatement contractor(s) must also prepare, separate from the scope of abatement work, an Operations and Maintenance (O&M) Plan which contains ongoing maintenance activities to be followed for as long as the LBP and/or asbestos remains in place. All abatement work and ongoing maintenance activities for LBP and/or asbestos shall conform to the following Regulatory requirements:

            (a) For LBP, 24 CFR Part 35.

            (b) For asbestos, 40 CFR Part 61.

         (2) The Lender must certify that the borrower has prepared an O&M Plan and that the Plan must remain in effect for the life of the mortgage.

         (3) A certification from the Lender to this effect is a mandatory condition for Firm Commitment and a required exhibit at Initial Closing.

   2. Special Requirements. Describe special work required for a specific item, room, space, unit or building.

B. All requirements must be specific and state the location, type and amount of work to be done without using general phrases, such as, “repair or replace” or “as required”.

C. In case of a gut substantial rehabilitation project, where only the structure will remain and the drawings and specifications will be as detailed as for new construction, the detailed work write-up need only be enough to be a basis for the cost estimate and to serve as a memorandum of understanding between the Hub/PC and the borrower.

D. Historic requirements including State Historic Preservation Office (SHPO) review, etc.

5.18 Contract Documents – Substantial Rehabilitation

The nature and extent of rehabilitation may vary widely among individual projects, and the requirements for specific contract documents cannot be determined by the Lender's architectural analyst until the joint inspection and work write-up are complete. When the contract documents are received, the Lender's architectural analyst must compare the documents to the detailed work write-up to confirm that the scope of work contained in the contract documents conforms to the scope of work in the detailed work write-up.

A. Drawings. When required, drawings must clearly define the concept and detail the rehabilitation, any demolition or removal, and the repairs and replacements.
   1. Require complete drawings and details similar to those for new construction if the structure will be gutted, or if there will be structural modification or an addition to the existing structure.
   2. For projects with minor changes in space arrangement, structural or mechanical systems, require only drawings sufficient to show existing conditions and the proposed work.
   3. Do not require drawings if the rehabilitation can be clearly and completely described in specification format.

B. Specifications. Work write-up/specifications are always required and must clearly define the scope of the rehabilitation, establish the quality of materials and workmanship, and the conditions of construction.

5.19 Engineering Reports – Substantial Rehabilitation

Surveys or special technical reports may be required of the borrower by the Lender for proper evaluation of the project and the Lender must:

A. Notify the borrower by letter immediately after the joint inspection of any requirement for such a report.

B. Clearly state the exact nature of the engineering or technical investigation and the items to be covered.

C. Specify any special tests, such as pressure or flow tests of plumbing or cutting of pipe, for examination.

D. Specify seismic resistance for substantial rehabilitation projects. Structures in seismic zones 3 and 4 must be capable of resisting 3/4 of the seismic forces contained in FEMA-310, Handbook for the Seismic Evaluation of Buildings – A Pre-standard, FEMA-356, Pre-standard and Commentary for the Seismic Rehabilitation of Buildings, and FEMA-274, NEHRP Commentary on the Guidelines for Seismic Rehabilitation of Buildings.

1. A seismic hazard analysis of the building(s) should be conducted by a registered engineer familiar with lateral force design, where applicable code requirements at the time of construction did not equal or exceed the referenced seismic standards.
2. The analysis should include an examination of the structure for continuity, ductility, and resistance to lateral forces.
3. Structural elements and connections between elements should be strengthened and retrofitted as required, if the existing structure does not provide 3/4 of the seismic force level resistance required, since the objective is to prevent major failures, collapse or loss of life due to earthquake forces.

E. A work write-up cannot be completed until all required engineering reports are analyzed by the Lender's architectural analyst and a determination has been made as to the need for additional rehabilitation that may be required.

5.20 Required Professional Services – Substantial Rehabilitation

The services of an architect or engineer, licensed to practice architecture or engineering in the state in which the project is located, are required for design and construction of a rehabilitation project when:

A. Working drawings and specifications are necessary to define the scope and concept of the rehabilitation,

B. Change of building use is proposed, existing spaces are to be altered, or structural changes are necessary, and/or,

C. An addition is proposed to the existing structure.

5.21 HUD Procedures - Pre-application Stage – Substantial Rehabilitation

A. The Lender must submit pre-application deliverables (Sections 5.6 and 5.15) to the Hub/PC.

B. In addition to procedures in Section 5.8.B, the HUD architectural analyst will examine the Basic Work Write-up and must issue a written report (Appendix 5F) containing recommendations and forward a copy to the Team Leader.

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.22 HUD Procedures: Firm Stage – Substantial Rehabilitation

A. The Lender must submit the Firm deliverables (Sections 5.6 and 5.15) to the Hub/PC.

B. In addition to the procedures in Section 5.9.B, the HUD architectural analyst must examine the detailed Work Write-up and must issue a written report (Appendix 5F.1) containing recommendations and forward a copy to the Team Leader. Where the project qualifies as substantial rehabilitation, the report must address each component and how it meets the "major building component" definition.

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

5.23 Section 223(f) – General

In general, all the previous instructions in this chapter applies to projects insured pursuant to Section 223(f), except as modified below.

5.24 Section 223(f) – Standards

Eligible properties are existing construction and the criteria for acceptance are not the same as for proposed construction. See Appendices 5C and 5D for architectural standards for 223(f) projects.

5.25 Section– 223(f) - Lender Deliverables

The Lender must present the following deliverables to the Hub/PC:

A. A complete Project Capital Needs Assessment and Replacement Reserve Escrow (PCNA) Report (see Appendix 5G) prepared by the Lender and described in Section 5.26.

B. Lender's review of the PCNA Report.

C. A completed A/E portion of Form HUD-92264. When the project consists of more than one structure, and where no architectural drawings are available, the Lender must prepare a Dwelling Unit Breakdown list, including unit count and unit areas, for each individual structure. In addition, the Lender must submit an estimate of the Gross Floor Area for each individual structure, based on the best estimate of the Needs Assessor.

D. Borrower's Exhibits. The borrower must submit the following exhibits for the Lender's architectural analyst to review:

1. Form HUD-92013.
2. Certificate of Occupancy or Final Inspection Report, if available or a statement from the jurisdiction of authority recognizing a conforming use.
3. Municipal Code Violation Report/Clear Report, and Fire Marshall's Report/Clear report.
4. City/County Health Officer's report/clear report where private water supply or sewage treatment systems are involved.
5. "As Built" Survey, Form HUD-92457M, Surveyor's Report; and Title Report. For specific survey requirements for Section 223(f) projects, see Appendix 5C, paragraph F.
6. Set of as built plans, if available.
7. Location map.

5.26 Section 223(f) - Project Capital Needs Assessment and Replacement Reserve Escrow

The Lender must prepare the PCNA and Replacement Reserve Escrow in accordance with Appendix 5G.

A. PCNA submission requirements.

1. Date of PCNA. The PCNA must be prepared and dated no earlier than 120 days prior to the submission of the application for Firm Commitment. The date of the PCNA is the date that the actual physical inspection of the property was performed.
2. Updating of PCNA. In the event that the Lender fails to submit an acceptable application for Firm Commitment within 120-days from the date of the original physical inspection, then the Lender must order an updated PCNA. The needs assessor must re-inspect the subject property, updating any structure and/or site conditions observed, and date and sign a new Third Party Certification.

B. PCNA content.

The PCNA consists of a Physical Inspection Report (PIR) and a Statement of Resources and Needs. The PIR contains detailed information about the condition of the project, its repair needs, expected repair and replacement needs over the life of the mortgage, and the inflation adjusted cost of those repairs and replacements. The Statement of Resources and Needs discusses the Lender's review of and possible adjustment to the PIR and identifies all critical repairs which must be completed before Initial/Final Endorsement and the associated cost of doing the work, as well as non-critical repairs to be completed after Final Endorsement and the associated costs to be escrowed.

C. Repair requirements.

1. All contemplated repairs, whether completed before or after Initial/Final Endorsement, must be fully described in the PIR, which is a required part of the PCNA.

2. No repairs may be started before the Section 223(f) application, including the PCNA, is submitted to HUD. After submission, repairs may not be started until HUD issues a Firm Commitment.
3. Requests to start repairs before the Firm Commitment is issued will not be accepted.

D. Repairs to be completed after Initial/Final Endorsement. If the borrower wishes to defer non-critical repairs until after closing, the following conditions must be met:

1. General.
   a. Only non-critical repairs may be deferred. Non-critical repairs are those that will not:
      (1) Endanger the safety and well-being of residents, visitors and passersby;
      (2) Adversely affect ingress or egress; or
      (3) Prevent the project from maintaining sustaining occupancy.
   b. Deferral of repairs may only be with the approval of the Hub/PC.
   c. Operating deficit escrow determinations must consider occupancy disruptions to any units and cash flow interruptions due to deferral of repairs.
   d. After Initial/Final Endorsement, work on deferred repairs must begin immediately.
2. Escrow Agreement for Non-Critical, Deferred Repairs (Form HUD-92476.1M) see this Form and Chapter 12 Section 12.17.A, for greater detail on these provisions.
   a. The costs of the deferred repairs (including materials, labor, permits, profits, etc., trended to the start of repairs) must be estimated and withheld ***in cash*** from mortgage proceeds and placed in escrow. A letter of credit may ***not*** be substituted for this escrow.
   b. An additional cash amount (or letter of credit, at the option of the Lender) of not less than 20 percent of the repair cost estimate will also be placed in escrow.
   c. The Lender may release funds from the mortgage proceeds portion of the escrow in proportion of the cost of work completed.
   d. Funds remaining in the escrow may be released when:
      (1) All repairs have been satisfactorily completed as determined by HUD;
      (2) Evidence of clear title has been provided to HUD; and
      (3) Latent defect assurances have been provided by the borrower (or the general contractor in cases where a construction contract, HUD-92442M was executed) by one of the following:
         (a) An escrow in cash, letter of credit or a surety bond from a surety, at the option of the Lender, equal to 2½% (or a greater percentage as warranted) of the repair cost maintained for 15 months from completion of repairs to cover situations where the

defect is discovered in the twelfth month and additional time is necessary to correct it.

(b) A Surety Bond in accordance with Form HUD-3259 from a surety on the accredited list of the U.S. Treasury for at least 2 ½ % of the repair cost, with the bond in effect for 2 years from the date of completion of repairs. See paragraphs 8 and 9 of HUD-92476.1M for further details.

3. Completion of Repairs.
   a. The Replacement Reserve Account shall not be used for the completion of any repairs, rehabilitation or construction items (see Appendix 5G, paragraph IV.A).
   b. The borrower must complete all repairs (see Appendix 5G, paragraph III.E) within 12 months of endorsement (or such shorter period as HUD and the Lender may specify).
   c. If the borrower has not completed all repairs by the end of the repair period (including any approved extensions), the Lender will complete the repairs using the escrowed funds and will provide the borrower with a breakdown of these repairs and the cost(s) of completion (including administrative expenses). Funds remaining in the escrow account after completion of the repair work will be returned to the borrower less reasonable administrative costs incurred in completing the repairs.
4. Requirements after Completion of Repairs. In cases where actual costs are less than estimated, the maximum insurable loan amount must be recalculated. If the maximum insurable mortgage is reduced due to lower actual costs, the borrower must prepay the mortgage:
   a. In amounts equal to the scheduled monthly principal payments, to the extent possible; with
   b. Any remainder going to the Reserve for Replacements Fund.
5. Exemption for Repairs for Tax-Exempt Bond Financed Projects. Project repairs which are required to satisfy tax code requirements but not required for Section 223(f) program compliance are exempt from Provisions 1 through 4 above, but must meet the following:
   a. The costs of the repairs cannot be considered in the determination of the value of the project or the computation of the maximum insurable mortgage.
   b. The repairs must not be necessary for the project (or for any unit in the project) to command the rent levels used in processing.
   c. The repairs must not delay or interrupt the occupancy of any unit in the project.
   d. Repairs must be paid from sources other than mortgage proceeds, secondary financing or the required repair escrows.
   e. Funds for these repairs must not be commingled with the Section 223(f) escrow.

E. Owner-Proposed Repairs and/or Improvements.

The needs assessor will classify all owner proposed repairs as critical or non-critical (see Appendix 5G).

5.27 Section 223(f) – HUD Procedures – Firm Stage

A. Lender must submit deliverables (Section 5.25) to the Hub/PC. The HUD architectural analyst will examine the Lender's PCNA Report, the underwriting summary and the borrower's exhibits and will review the quality of the Lender's report and the transaction itself. The HUD analyst will not reprocess the case. However, if the HUD analyst determines that certain underwriting conclusions are not supportable and affect HUD's risk, the analyst may recommend that the Lender modify the application or may recommend a rejection. The Team Leader will approve, reject or modify the recommendation of the HUD architectural analyst.

B. The HUD architectural analyst will review the deliverables noted on the review report and will report to the Team Leader on the form at Appendix 5F.2, recommending either acceptance or rejection of the A/E portion of the submission, based on a comparison of selected areas of concern in the PCNA Report with the Borrower's Exhibits. At a minimum, the HUD architectural analyst will consider Critical Repairs covering health and safety (and accessibility for persons with disabilities for projects built after March 13, 1991).

5.28 LIHTC Streamlined Processing Instructions

The current MAP policy requires the submission of complete and final architectural Drawings and Specifications with the Firm Commitment For applications for projects involving LIHTCs, the submission of final project drawings and specifications may be deferred until Initial Endorsement. Other modifications are as follows:

A. Schematic drawings may be submitted in lieu of complete and final plans and specifications with the Firm Commitment application.

B. Lenders and Hub/PCs must review the level of experience of all development team members and must determine that only those with adequate knowledge of HUD's development, design and building requirements are acceptable for this streamline process. Hub/PCs should also consider the complexity of the proposed design and construction when determining whether to permit the deferred submission of final drawings and specifications.

C. Hub/PCs should determine that the project will achieve initial closing within 60 days after issuance of a Firm Commitment conditioned upon final plan submission. In addition, full and final plans must be submitted 30 days prior to the scheduled Initial Endorsement to provide time for HUD review and approval.

D. The Firm Commitment may be conditioned on the timely receipt and satisfactory review of complete and final plans and specifications, subject to the conditions outlined below:

The Lender's submission of less than 100% of the Drawings and Specifications (i.e., schematic/line/working drawings) must provide the following detail:

1. The static footprint of the building as it rests on the surveyed site plan.
2. The gross building and net residential footage.
3. Unit layouts for each major unit type.
4. Sufficient design detail to make a Davis-Bacon Wage rate classification determination.
5. Sufficient design detail to determine compliance with accessibility requirements in Appendix 5.
6. A written cost estimate (HUD-2328) from the general contractor proposed to participate in the project.
7. For Pre-applications: Exhibit 5 of Appendix 4A.
8. For Firm Commitment applications: Exhibits A.16, 17, 24, 25, 27, and B.3 of Appendix 4A, as applicable.

E. Scope of HUD Review and determinations required in order to issue a Firm Commitment:

1. An assessment that the estimated project cost based on Form HUD-2328 is reasonable and in line with comparable HUD LIHTC project data;
2. An assessment that the proposed general contractor is acceptable pursuant to outstanding requirements (sufficient working capital, experience, etc.); and
3. An assessment that the sketch plans are in compliance with all applicable requirements on a preliminary basis, with appropriately qualified certifications executed.

D. A modification must be made to the commitment for those projects determined to be eligible for the submission of deferred plans. Below is a sample special condition to be added to the Firm Commitment.

"As an accommodation, this commitment has been issued and based upon schematic drawings, instead of the final drawings and specifications. At least 30 days prior to the scheduled date for Initial Endorsement, Hub/PC must receive the final drawings and specifications for review and approval to ensure consistency of design and cost. In the event that there is a net cumulative construction cost increase or change in the design concept, or a net cumulative construction cost decrease in the amount of more than 2%, this commitment shall be subject to and conditioned upon the further approval of HUD, to be evidenced in writing, and may be terminated and voided by HUD, or additional conditions may be imposed, at HUD's option."

The Phase I (ASTM Practice E 1527-06 or most current) environmental report must contain no significant unresolved environmental issues that would justify a Form HUD-4128 "Environmental Assessment & Com."

Chapter 6

Cost Processing

6.1 Qualifications, Responsibilities, and Approval of the Lender's Cost Estimator

A. Qualifications of Lender's Cost Estimator - The Lender must hire a qualified construction cost estimator with experience in multifamily cost estimating and with knowledge and experience with local building standards and construction costs for the type of project proposed. A cost estimator may also serve as the architectural analyst if the qualifications are met.

B. Responsibilities of Lender's Cost Estimator - The cost estimator must provide an independent cost analysis for the proposed project. This estimate is not limited to any one specific method. However, the method chosen must be one recognized by the construction industry. This detailed cost estimate must conform to HUD's line item format as shown on Form HUD-2328, Contractor's and/or Borrower's Cost Breakdown.

HUD Approval of the Lender's Cost Estimator - The Department reserves the right to examine the credentials of all cost estimators hired by the Lender, and to reject any and all individuals that it considers unqualified.

6.2 Section 220, Section 221(d), and Section 231 Lender Responsibilities and Deliverables

A. Responsibilities

A complete construction cost analysis must be submitted with the Firm Commitment application. The Cost Analyst's responsibilities are:

1. Preparation of detailed project cost estimate.
2. Completing Cost portions of Form HUD-92264, Project Income Analysis and Appraisal.
3. Reviewing and approving or disapproving the Contractor's and/or Borrower's Cost Breakdown, Form HUD-2328.
4. Preparation of Form HUD-92329, Property Insurance Schedule. Note that Form HUD-92447, Property Insurance Requirements, will be prepared by HUD and provided to the Lender at closing. (See MAP Forms Book.)
5. Reviewing and approving or disapproving requests for prior approval of identity of interest subcontractors.
6. Estimate costs of Replacement Reserve items (for substantial rehabilitation or where the formula based reserve-for-replacement has been waived). Note that there is no initial Replacement Reserve for complete substantial rehabilitation (see Chapter 7).

7. Providing advice and assistance on cost matters to borrowers, consultants, contractors, and others.

B. Deliverables

1. Firm Stage - Cost Estimate Package:

   a. Detailed Cost Estimate. To be reported on Form HUD-92326:

      (1) Detailed structure(s) and land improvement cost estimates, for new construction and substantial rehabilitation, and costs of unusual site development.

      (2) Contractor's General Requirements, General Overhead and Profit, and Architect's Design and Supervision fees.

      (3) Bond Premium and Borrower's and Contractor's Other Fees.

      (4) Onsite Demolition costs.

      (5) Off-site improvement costs.

      (6) Project's Cost Not Attributable (CNA) to dwelling use.

   b. Preparation of Cost portions of Form HUD-92264, Project Income Analysis and Appraisal, signed by Lender's cost analyst under "Cost Processor."

   c. Preparation of Form HUD-92329, Property Insurance Schedule. Note that Form HUD-92447, Property Insurance Requirements, will be prepared by HUD and provided to the Lender at closing. (See MAP Forms Book).

   d. Review the Contractor's and/or Borrower's Cost Breakdown, Form HUD-2328:

      (1) Submit the Contractor's and/or Borrower's Cost Breakdown.

      (2) Review the Contractor's and/or Borrower's Cost Breakdown and recommendation for approval or disapproval. Review must include a trade line item comparison of Form HUD-2328 and the estimator's cost estimate (Form HUD-92326), which is to be provided on Form HUD-92331.

      (3) Signatures. The Lender's cost analyst must sign and date Form HUD-2328 in the FHA: Processing Analyst box. The Lender's Underwriter must sign and date Form HUD-2328 in the FHA: (Chief, Cost Branch or Cost Analyst) box. The FHA (Chief Underwriter) line will be endorsed by both the HUD cost reviewer and the HUD Team Leader.

   e. For substantial rehabilitation (in addition to the above):

      (1) Joint work write-up;

      (2) Replacement Reserve estimate (see Chapter 7);

   f. Reserve-for-replacement analysis where the formula has been waived.

2. Identity of Interest and 50-75 Percent Rule Disclosure. (See Chapter 13 Section 13.15 for 50-75 Percent Rule instructions.)
   a. Identification of any identity of interest relationship(s) between or among:
      (1) Borrower,
      (2) Borrower's Architect,
      (3) General contractor,
      (4) Subcontractor(s),
      (5) Material supplier(s),
      (6) Equipment lessor(s),
      (7) Manufacturer(s) of industrialized housing.
   b. Identification of any subcontractor(s) that violate the 50/75 Percent Rule by analysis of Form HUD-2328.

C. Additional instructions for streamlined processing of LIHTC applications are in Section 5.28.

6.3 The Lender's Cost Estimate

The replacement cost estimate is one of the criteria used to determine the mortgage amount to be insured. It consists of estimates of the new construction and/or substantial rehabilitation costs of all proposed improvements to the property.

A. Method of Estimation. The method should be similar to that used by general contractors. Data should be organized by trade division using the Construction Specification Index (CSI) Format, and adjusted to reflect cost differences due to time, location and price fluctuations. The cost estimate may be prepared using a quantity survey takeoff or a square-foot and per-unit cost approach using established data and making adjustments.

B. Data. The data source used to prepare the cost estimate must be documented. Acceptable cost data may come from completed comparable projects, benchmark amounts taken from actual project costs, and published data from construction cost data publishers.

C. Detailed Cost Estimates. Use detailed plans and specifications supplied by Lender's architectural analyst as required by Section 5.5, as a basis for the cost estimate. Estimates must reflect the general level of construction costs in the locality where construction takes place. Costs must be projected to the estimated construction start date. Davis-Bacon labor wage rates must be used. (It is the project architect's responsibility to obtain current Davis-Bacon wage rates from HUD. See Section 5.4). The cost estimate is tabulated on Form HUD-92326, and totals are reported in Sections G, M, and O of Form HUD-92264. (See MAP Forms Book for all HUD forms). The cost estimate consists of the following items:

   1. Structures and Land Improvements include:

a. Dwelling structures. Costs of all residential buildings including footings and foundations. Costs must be organized in the Construction Specification Index (CSI) trade item format. Report trade costs in Divisions 3 through 16 on Form HUD-92326.

b. Garages include all covered parking, from individual carports to complete parking structures. Include free-standing garage structures with other accessory buildings on the Accessory Structures line on Form HUD-92326. On Form HUD-92264, garages are reported separately on Line G.39.

   Exception: Where a garage structure serves as a base for the dwelling structure (common practice in high-rise reinforced-concrete apartment buildings), include the garage trades with the Dwelling Structure trade items; do not report separately on either Forms HUD-92326 or HUD-92264.

c. Accessory buildings. Include costs on the Accessory Structures line on Form HUD-92326 and on Line G.38 of Form HUD-92264.

   Exception: Where accessory uses are not placed in a separate building but rather occupy space within the residential structure(s), include the spaces within the Dwelling Structure trade items; do not report separately on either Form HUD-92326 or HUD-92264.

   (1) Community structures include non-residential uses intended for all project residents but not open to nonresidents. These include clubhouses, meeting halls, exercise rooms, etc.

   (2) Commercial structures include non-residential, commercial uses that derive their income from both project residents and the general public.

d. Onsite land improvements make up the following trade line items on Form HUD-92326: Earthwork, Site Utilities, Roads and Walks, Site Improvements, Lawns and Planting, and Unusual Site Conditions.

   (1) Unusual land improvements are items not typical to most construction in the locality such as, excessive excavation, rock excavation, cuts and fills, special foundations, high water table, problem soils, etc. These items are taken from the Unusual Site Conditions trade line item on Form HUD-92326, and are reported separately on Line G.36a of Form HUD-92264. A cost analyst works with the appraiser to determine existence of condition.

   (2) Other land improvements are the typical site-work items (Earthwork, Site Utilities, Roads and Walks, site Improvements, Lawns and Plantings) taken from the Land Improvement trade line items on Form HUD-92326, and are reported on Line G.36b of Form HUD-92264.

e. Offsite extensions of roads, walks, and utilities immediately adjacent to project boundaries. See Section 6.3 C.2.b. (2) below for more details.

2. Supplemental Cost Estimates include:

a. Demolition. This is onsite work to remove existing structure, footings, foundations, and utilities to prepare the site for new construction.

(1) Include the removal and disposal of debris and fill and compaction of excavations. Include general contractors' and subcontractor's overhead and profit in the estimate.

(2) Report on Form HUD-92326, under "demolition," and Form HUD-92264, Section O. Appraiser will report Demolition costs in Section J of Form HUD-92264.

(3) Demolition should not be included in the construction contract.

(4) Outside demolition does not include interior demolition within existing structures undergoing substantial rehabilitation. See Section 6.6.B.1.b. (1)(a).

b. Offsite work that is not immediately adjacent to project boundaries.

(1) Include utilities, walks, curbs, gutters, streets, drainage structures, landscaping, etc., that extend away from the project site. These improvements are not included in the construction contract. Report on Form HUD-92326 and Section M of Form HUD-92264.

(2) Do not include short offsite extensions of onsite utilities, walks, curbs and drainage structures that connect with those immediately adjacent to the project site. These short extensions, and improvements such as sidewalks and curbs adjacent to the property lines, should be considered onsite improvements and included in the construction contract.

3. Cost Not Attributable to Dwelling Use (CNA) consists of certain project amenities and uses other than dwelling uses. CNA is calculated by the cost analyst and used by the appraiser to increase the maximum mortgage amount under Criterion 4 of Form HUD-92264-A. Include these costs within the estimate of total structures and land improvements; also itemize the costs and report separately in Form HUD-92326 and Section M of Form HUD-92264.

a. CNA for new construction.

(1) For new construction projects, CNA is calculated as a percentage. The CNA percentage consists of the ratio of the cost of the non-attributable spaces and facilities (abbreviated "B") to the total cost of land improvements and structures (abbreviated "A"), known as the B over A ratio, or simply B over A.

(2) B over A Ratio. Costs are generally based on gross floor area of the building, area of exterior site improvements, and/or lump sums.

(a) To calculate "B" costs:

(i) Prepare a worksheet describing by category each item considered in CNA, showing the calculation of the cost of each item. Do not include General Requirements or fees in the calculation.

(ii) Show the basis of measurement and the unit price.

(iii) Summarize the categories and total in Form HUD-92326 and Section M of Form HUD-92264.

(b) To calculate "A" costs:

(i) "A" is the sum of Total Structures and Total Land Improvements, before General Requirements or fees are added. To calculate "A", add the amounts in lines 36c and 41 in Section G of Form HUD-92264.

(c) To calculate B over A:

(i) Divide the "B" costs by the "A" costs. Express as a percentage and enter in Section M of Form HUD-92264.

(d) For a complete example of calculating CNA, see Appendix 6D.

b. CNA for substantial rehabilitation.

(1) CNA for substantial rehabilitation projects is determined in a different manner from CNA for new construction. Under this method, CNA rehabilitation work, and "as is" CNA value, are combined to produce a single dollar amount. For determining Rehabilitation CNA Fee, see the worksheet in Appendix 6C and the example in Appendix 6D.

(2) Open-air parking lots and other open air CNA uses in a substantial rehabilitation project. A procedure has been developed to prevent open-air CNA uses covering large site areas, such as parking lots, tennis courts, etc., from distorting the amount of Rehab CNA. See the Rehab CNA worksheet in Appendix 6C and the example in Appendix 6D.

c. CNA Categories. There are two main CNA categories, Residential and Commercial. Each is calculated independently of the other and each has a maximum limit of 15%, resulting in a total CNA of up to 30% (see the example in Section 6.3.C.3.d). Every CNA use must be categorized either as Residential or Commercial, <u>but not both.</u> Note: Any request to waive these limitations must be documented and justified in accordance with the provisions of Chapter 11 Section 11.2.

(1) Residential CNA. This consists of non-attributable items solely for the use of residents of the project. Items to consider as not attributable to dwelling use are:

(a) Parking areas and the walks and driveways specifically leading to them and serving them. Do not include public roads and streets, or walks and driveways that lead to and serve the building entrance.

(b) Garages, garage spaces, and covered parking, and the walks and driveways leading to them, excluding public roads and streets.

(c) Other improvements include**:**

(i) Community space, such as: multipurpose rooms, game rooms, lounges, libraries, and hobby or craft rooms, including furniture or movable equipment.

(ii) Project administrative and maintenance spaces, such as: offices, repair shops, employee toilets, and janitor or cleaning closets, including furniture or movable equipment.

(iii) Storage facilities that are <u>not</u> for occupant use.

(iv) Recreational facilities, such as: swimming pools, tennis courts, basketball courts, and tot lots, including furniture or movable equipment.

(v) Works of art that are fixed in place, such as wall murals or permanent ornamental fountains.

(d) Special Exterior Land Improvements are features unusual or in excess of those typical in projects for similar occupancy.

(i) Include such items as patios, sitting areas, and gazebos for the use of all project occupants. Include fountains and pools, exterior works of art, unusual trees and shrubs, and ornamental lighting and fencing.

(ii) Do not include typical earthwork, roads and walks leading to and serving the dwellings, typical lawns and plantings, private balconies and patios, utility lines, retaining walls, or security lighting and fencing.

(2) Commercial CNA

This consists of areas or buildings and improvements intended for the use of the public as well as project residents. The most common commercial uses in residential developments are:

(a) Shops,

(b) Offices, and

(c) Public parking.

Include only the basic and permanent structural improvements typical in vacant commercial space. Do not include equipment, fixtures, movable partitions, special finishes, etc., for a specific business.

d. Limitation on CNA

(1) Residential CNA: The B over A ratio for residential CNA should not exceed 15%. This is exclusive of any commercial space in the project, which will have a separate commercial CNA.

(2) Commercial CNA. Commercial CNA applies to commercial space such as shops that are in a residential structure, but serve the general public as well as the residents. This is calculated separately from residential CNA. The B over A ratio for commercial CNA should not exceed 15 percent. The Lender's underwriter should be aware of the higher risk inherent in commercial space and take special care to evaluate the commercial market in order to determine the maximum commercial space that can be included in the project without imposing undue risk**.**

Example: A project has residential CNA of 12% and commercial CNA of 7%. Each CNA category is within the 15% guidelines. Total CNA for the project is 12% residential plus 7% commercial, equaling 19%.

(3) CNA Limits for Substantial Rehabilitation projects: Regardless of the method of determining Rehab CNA, there is a CNA ceiling for sub rehabilitation.

Use the B over A ratio to determine the CNA ceiling for sub rehabilitation, the same as for new construction. Even though B over A is not to be used for actual dollar amounts for sub rehabilitation projects, it is a legitimate tool for determining a CNA ceiling for sub rehabilitation. Use 15% as the ceiling for residential CNA rehabilitation work and another 15% as the ceiling for commercial CNA rehabilitation work.

Note that, in a sub rehabilitation project, the cost ("B") of the non-attributable rehabilitation work does **not** include the "as-is" value of the existing CNA use. The cost ("A") of the total rehabilitation work includes all structures rehab work and land improvement rehabilitation work, but **not** any "as-is" value.

When a project contains both residential and commercial CNA, and both residential and commercial CNA are determined to be acceptable using the above B over A tests, the residential and commercial CNA may be combined in a single Rehab CNA procedure. See the example in Appendix 6D.

e. Items not to be included in CNA:

(1) Dwelling units. No portion of any dwelling unit, or any balcony or patio solely for the private use of the resident of the individual dwelling unit, is to be included in CNA**.**

(2) Utility rooms. Do not include utility rooms or portions of basements devoted to utilities such as boilers or furnaces, hot water heaters, water and sewer mains, gas mains, or electrical panels or closets.

(3) Circulation elements. Do not include entrances, lobbies, halls, corridors, stairs, and elevators used by the occupants to enter and leave dwelling units. Do not include roads and walks that lead to and serve the dwellings.

(4) Prorating of circulation elements. A prorating of circulation elements between dwelling use and any category in CNA is not permitted.

(5) Minor movable items that are not part of the real estate

(6) For commercial CNA, do not include equipment, fixtures, movable partitions, special finishes, etc., for a specific business.

4. Allowances and Fees are reported on Forms HUD-92326 and HUD-92264 as lump sum dollar amounts. Depending upon data, they may be calculated either as lump sums, or as percentages of subtotals which are converted to dollar amounts.

   a. General Requirements (Job Overhead). Covers project specific overhead expenses. Calculate as a percentage of the sum of Total Land Improvements and Total Structures. The percentage amount is determined by the nature, difficulty, size of the project, and the characteristics of the neighborhood.

      (1) Include:

         (a) Supervision and job-site engineering;

         (b) On-site job office expenses directly related to the project including clerical wages;

         (c) Temporary buildings, tool sheds, shops, and toilets,

         (d) Temporary heat, water, light and power for construction;

         (e) Temporary walkways, fences, roads, siding and docking facilities, sidewalk and street rental;

         (f) Construction equipment rental not included in trade item costs;

         (g) Cleanup and disposal of construction debris;

         (h) Medical and first aid supplies and temporary facilities;

         (i) Security guard wages and related costs;

         (j) Theft and vandalism insurance. (does not include Builders Risk Insurance).

         (k) Builders Risk Insurance may be included with general Requirements or Contractor's other fees (only if paid for by General Contractor).

         Builders Risk Insurance is separate from any theft and vandalism insurance policy taken out by the general contractor. While Builders Risk Insurance may be taken out either by the general contractor or the Borrower, it is common industry practice for the contractor to take out the policy, with the contractor named as Insured, and the Borrower named as "Other Insured." Regardless of which party pays for the policy, the Borrower must always be named as an

Insured party, as per Builder's Risk Insurance requirements in Form HUD-92447, Property Insurance Requirements. If the contractor pays for the policy, the premium belongs in the construction contract under General Requirements. However, if the Borrower pays for the policy, the insurance premium belongs under Insurance on Line G-55, Insurance, of Form HUD-92264.

(2) Do not include salaries of owners, partners, or officers of the general contracting firm when they visit the site. This is included in General Overhead. The only exception would be actual work done on the job by these individuals in a trade capacity, as laborers or supervisors.

b. General Overhead. Covers contractor's head office and general business expenses. Amount is fixed at 2 percent of the sum of Total Land Improvements, Total Structures, and General Requirements.

c. Builder's Profit. Calculate as a percentage of the sum of Total Land Improvements, Total Structures, and General Requirements. Percentage amount is determined by the nature and location of the project.

(1) BSPRA. Builder's and Sponsor's Profit and Risk Allowance (BSPRA) applies to projects where there is an identity of interest between the borrower and the general contractor. BSPRA is limited to Section 220 and Section 221(d) (4) projects with such an identity of interest. The appraiser calculates the BSPRA amount and enters it on line G 68 of Form HUD-92264. Where BSPRA applies, do the following:

(a) Calculate an equivalent builder's profit and an equivalent subtotal.

(b) On the Builder's Profit line of Form HUD-92326 and on Line G 44 of Form HUD-92264, enter the word "BSPRA". The equivalent builder's profit calculated above is not included in the Total for All Improvements (bottom of Form HUD-92326 and Line G.50 of Form HUD-92264).

d. Architect's Fees. Source is Owner-Architect Agreement, AIA Form B-108, to be provided to Lender's estimator. In the event of multiple prime contracts (e.g. engineers), total in line G 45 of HUD-92264 and itemize in Section O, Remarks. Estimator should copy the fee amounts, unaltered, to the cost estimate. Estimator should document architect's fees and compare with existing fee data to determine reasonableness. Estimator should inform the Lender if fees are significantly different from the data range, but the fees should not be altered on the cost estimate without a prior meeting between the Lender, Lender's estimator, borrower, and project Architect. Fees should be documented as a percentage of the sum of Total Land Improvements, Total Structures, General Requirements, General Overhead, and Builder's Profit (equivalent Profit in BSPRA cases).

The Architectural Design Fee covers preparation of all construction documents (working drawings and specifications) up to start of construction. (Usually 75 to 80 percent of total) And, the Architectural Supervision fee covers, covers the Architect's construction

inspections, reports, and preparation of change order requests. (Usually 20 to 25 percent of total).

e. Bond Premium. This covers Performance Bonds used to ensure completion of construction in event of a default by the general contractor. Bonding company determines applicable rate by the nature and location of the project and the contractor's history.

f. Other Fees. Costs of various required items and services. They can vary greatly from community to community. They can be paid either by the borrower or the general contractor. The borrower may submit an itemized list with costs as an aid to the cost estimator. The Other Fees can include:

(1) Site and topographic surveys,

(2) Subsurface exploration (test borings),

(3) Soil tests, concrete tests, and other construction testing,

(4) Fees for utility taps and connections,

(5) Building permits and licenses, and

(6) General Contractor's cost certification audit fee (if required).

NOTE: The borrower's cost certification audit fee is not to be included in Other Fees since it is recorded separately on Line G. 66 of Form HUD-92264.

(7) Builders Risk Insurance may be included with general Requirements or Contractor's other fees (only if paid for by General Contractor).

g. Furniture, Fixtures, and Equipment (FF&E) includes substantial indoor and outdoor furniture and equipment. It may not include titled vehicles, minor items of relatively insignificant cost such as furniture accessories, income from rental unit furnishings, hand tools and hand power tools, or expendable items. An itemized schedule of FF&E with cost for each item will be submitted with the cost documents and reviewed by the Lender's cost analyst for acceptability as FF&E and cost. Cost may include delivery and placement, but without any other fees. The dollar amount of FF&E will be reported on line G.60 of the HUD-92264; "AMPO percent (nonprofit only)" will be lined out and substituted with "FF&E".

5. Construction Time is measured in months and varies depending upon the size, complexity, location and type of construction. When documenting estimated construction time, it is recommended that graphs be established for each project type and structural system and should indicate the number of dwelling units and number of months to construct. Report construction time frame on Line G. 52 of Form HUD-92264.

D. Property Insurance Schedule and Requirements

1. The Property Insurance Schedule (Form HUD-92329) documents the 100% Insurable Value of the project structure(s). See MAP Forms Book for HUD-92329 preparation instructions.

2. Property Insurance Requirements (Form HUD-92447) accompanies the Property Insurance Schedule and is prepared by HUD and provided to the Lender at closing. It serves as an official advisory to the Lender of the requirements for the types of Property Insurance that must be maintained on the property and of the estimate of the Total 100% Insurable Value of the property. See MAP Forms Book for an example of Form HUD-92447.

E. For new construction or substantial rehabilitation projects, the minimum reserve-for-replacement deposit will be the higher of:

1. the amount required by the Section 221(d)(4) program, or
2. $250 per unit per year

In order to avoid over-funding reserve-for-replacement accounts for high-cost properties with low reserve-for-replacement needs, waivers of the formula based calculation of reserve-for-replacement deposit will be considered if the formula approach results in a per unit per annum deposit requirement of greater than $500. The Multifamily Hub Director's approval of a waiver request must be supported by the Lender's third-party Architecture, Engineering and Cost Analyst documentation and conclusion that a lesser amount is justified.

Projects must obtain a new PCNA every 10 years with the reserve-for-replacement deposit adjusted based on the results of the PCNA. The Lender will create a schedule that is analyzed for the life of the loan. Particular scrutiny should be given to the first 15 years. HUD Asset Management staff must review and concur or non-concur on the deposit requirements. Development staff will consider this determination and make a final determination of the reserve requirements. The reserve schedule and deposit requirements required by the Firm Commitment will be applicable during the first ten year term of the mortgage.

6.4 Project Processing – Pre-Application Stage

HUD will perform processing according to Section 6.7 and additional instructions for streamlined processing of LIHTC applications in Chapter 5 Section 5.28.

6.5 Lender's Project Processing – Firm Stage

At this stage, the Lender's cost estimator will prepare a detailed cost estimate and all required reports and recommendations indicated below:

A. Forms to Use

1. Form HUD-92326. Used for preparation of detailed construction cost estimate.
2. Form HUD-92331-B. Used to make detailed comparison of trade line items between Estimators' cost estimate (HUD-92326) and Contractor's trade payment breakdown (HUD-2328).

3. Form HUD-92329. Property Insurance Schedule, used to determine the Maximum Insurable Value for all project structures. Note that Form HUD-92447, Property Insurance Requirements, will be prepared by HUD and provided to the Lender at closing.
4. Form HUD-92264. Project Income Analysis and Appraisal.
   a. Section G. Estimated Replacement Cost, Line 36a through 52, used to summarize Total Structures, Land Improvements, General Requirements, and Fees from Form HUD-92326. Also records Estimated Construction Time.
   b. Section M. Used to summarize Cost Not Attributable to Dwelling Use (lines 10 through 15), and Offsite Requirements (lines 16 and 17).
   c. Section O, Remarks. Used to explain Unusual Land Improvements, Other Fees, itemization of professional fees (e.g. engineers), overall difference between Lender's and borrower's cost estimates, and other cost items.

B. Prepare detailed cost estimate on Form HUD-92326 using instructions in Section 6.3. Sign form on the "Estimate Prepared by" line and certify. See standard certification in Chapter 11, Section 11.2. The Lender's architectural analyst will supply detailed plans and specifications as indicated in Chapter 5, Section 5.5.

C. Resolve differences in Lender's and contractor's construction cost estimates.

   Before the Firm Commitment application can be submitted for HUD review, there must be a general agreement between the construction cost estimates prepared by the general contractor and the Lender's cost estimator. The Lender's cost estimator is responsible for resolving major differences between the two estimates. When the two estimates generally agree, the Lender may use the contractor's cost figures as shown on Form HUD-2328 as its cost estimate. The Lender's cost estimator will use the following review procedure:

   1. Prepare trade line item comparison of Lender's and contractor's cost estimates using Form HUD-92331-B.
      a. Enter costs from Forms HUD-92326 and HUD-2328. For multiple-structure type projects, a separate HUD-2328 must be submitted for each structure type, and a master HUD-2328 for the entire project.
      b. Calculate and list line item percentage differences.
   2. Review trade line item differences and note all variations beyond normal ranges. The range of trade line item differences varies from trade to trade. Major trades (e.g. engineers, carpentry) should have a smaller range difference than minor trades (e.g. sheet metal). The estimator should judge the variations based on established data.

      Front-end Loading: The estimator should be alert for a pattern of front-end loading in trade items, where the contractor inflates the first few trade item costs in order to secure more mortgage proceeds early on in construction. Such a pattern may indicate inadequate working capital or risky business practices on the contractor's part. Front-end loading can jeopardize the construction of the project, especially since the contractor must under-estimate later trades in order to balance out the bottom line of the estimate, making these later trades especially vulnerable to shoddy work practices and even outright default.

3. Meet with contractor to discuss and resolve all questionable trade line item differences. Resolution process may result in either the estimator or the contractor, or both, recalculating costs of various trade line items based on discussions.
   a. If differences are resolved, accept costs in Form HUD-2328 and use as Lender's Cost Estimate in Form HUD-92264.
   b. When dealing with suspected front-end loading, require rigorous documentation of early trade items that are higher than normal.
   c. If differences cannot be resolved, do not accept costs in Form HUD-2328.
      (1) Use estimator's cost estimate as Lender's cost estimate.
      (2) Inform the Lender's underwriter that the contractor's HUD-2328 is unacceptable.
      (3) Advise the Lender's underwriter to meet with the borrower and the contractor for further attempts at resolution.

D. Prepare cost portions of Form HUD-92264, using instructions in Section 6.3. Sign form in the "Cost Processor" box and certify (see standard certification in Chapter 11, Section 11.2).

E. Property insurance schedule, Form HUD-92329, provides a guide for the amount of insurance coverage. Note that Form HUD-92447, Property Insurance Requirements, will be prepared by HUD and provided to the Lender at closing. (See MAP Forms Book for HUD-92329 preparation instructions and an example of Form HUD-92447).
   1. Prepare form at submission of Firm Commitment package.
   2. Estimate 100% insurable value for each building.
      a. Include cost of structures, foundations and basement, underground utilities within the building walls, and a proportionate share of allowances and fees, except for Other Fees.
      b. Do not include the cost of land improvements, onsite demolition, or offsite work.
      c. Include the cost of major mechanical equipment, such as boilers serving the entire project, in the cost of the building where the mechanical equipment is located.

F. Prior approval of identity of interest subcontractors' amount including overhead and profit.
   1. Identity of Interest is a relationship that exists giving the borrower or general contractor apparent control or influence over a subcontractor, equipment lessor, material supplier, or manufacturer of industrialized housing. (See General Contractor's cost certification instructions in Chapter 13 - Cost Certification, for definition of relationships).
   2. Requirements. When subcontractors, material suppliers, or equipment lessors have an identity of interest with a borrower or general contractor, the Lender must approve the subcontract amounts, including specific amounts for subcontractor general overhead and profit.
   3. Timing. Approval is required before work begins under the subcontract. Failure to secure prior approval will result in the disallowance of the total general overhead and profit of the subcontractor at cost certification.

4. Request for approval (with the subcontracts, agreements, or leases) goes to the Lender's cost estimator, whose recommendations must cover:
   a. Acceptability of the documents.
   b. Reasonableness of guaranteed maximum prices for the subcontract work.
   c. Appropriateness of general overhead and profit dollar amounts.
5. Mandatory Conditions for Approval.
   a. Subcontracts:
      (1) There must be a separate one for each trade.
      (2) Subcontract must clearly identify scope of work.
      (3) Be on a cost plus fixed fee basis:
         (a) Guaranteed maximum dollar amount for work.
         (b) Specific dollar amount for general overhead and profit.
      (4) Disapprove "paper conduit" arrangements where work is to be done by general contractor personnel or other subcontractors, suppliers or lessors.
   b. Subcontract prices: For this criterion, recent reliable data is a better test than whether higher bids were submitted.
      (1) The total price must not exceed the amount shown for the trade item on the accepted Form HUD-2328.
      (2) Total price must not exceed reasonable prices taken from available data.

      NOTE: The Lender's cost analyst must resolve disagreements in trade prices with the subcontractor.
   c. Overhead and Profit. The amounts for general overhead and profit shall be no higher than the typical prices for the specific trade.
   d. Subcontractor entity. The burden of proof of 1, 2, and 3 below is on the subcontractor.
      (1) The firm must operate and have documented experience as a subcontractor for the specific field covered in the subcontract.
      (2) Must control labor, materials, and equipment typical for the trade.
      (3) Must do significant business in its specific field with borrowers and general contractors having no identity of interest.
6. If total of all identity of interest subcontracts, purchases and leases is less than ½ of 1 percent of the mortgage amount, the requirements for each identity of interest subcontractor to cost certify may be waived by the Hub Director upon notification by the Lender.

7. Prepare letter of approval or disapproval to the borrower or general contractor. Letter must address all mandatory conditions.
   a. Approval will indicate any conditions, including whether or not subcontractor must cost certify.
   b. Disapproval will state the reason for disapproval and indicate any cost certification requirements.

6.6 Lender's Processing – Substantial Rehabilitation

A. General. In developing the cost estimate for substantial rehabilitation, follow the instructions of other sections of this chapter, except as modified by the following:

B. Firm Stage:

1. Rehabilitation cost estimate:
   a. Borrower's Cost Exhibits. Detailed plans, specifications, and scope of rehabilitation work supplied by Lender's architectural analyst as required by Chapter 5 Sections 5.5 and 5.14, and general contractor's Form HUD-2328.
   b. Lender's cost estimator will do the following:

      (1) Using the construction drawings and specifications, the scope of work indicated in the joint work write-up and applicable data (all supplied by the Lender's architectural analyst), the Lender's cost estimator will prepare a detailed cost estimate. Estimate must include quantities and unit costs for all items described in the joint work write-up. Include the following items that are specific to substantial rehabilitation:

         (a) Interior demolition and removal of floors, walls, roofs, doors and windows, finishes, cabinets, appliances, plumbing, HVAC, and electrical, including boilers and central air conditioning. Also includes abatement of asbestos and lead based paint. Enter amount in Special Construction trade line in Form HUD-92326. If individual trades include removal (e.g. remove and replace cabinets), removal costs may be included in the trade line item.

         (b) Onsite demolition is not part of the Construction Contract and should be estimated and recorded in the same way as for new construction (see Section 6.3).

         (c) Allowances and Fees for substantial rehabilitation, especially General Requirements and Architect's Fees, are calculated the same way as for new construction, but they should reflect the risk and responsibility inherent in rehabilitation and consider the location of the project. Recommend that the cost estimator keep separate data for this item.

         (d) Rehabilitation time is determined the same way as construction time for new construction, but the data used must take into account the time required for

interior demolition, as repair and rehabilitation cannot begin until such demolition is complete.

(e) Rehabilitation cost not attributable to dwelling use includes an "as-is" value for non-attributable items in addition to a value for actual work performed. Calculate by using the format in the Appendix 6C. The cost analyst completes steps 1, 2, and 3, steps 4 through 8 are completed by the appraiser.

(f) Contingency reserve amount is based on available data for the type and condition of structure. Calculate as percentage of the sum of structures, land improvements, and general requirements. Percentage ranges from 10 to 15%, depending on the condition of the project, extent of rehabilitation, and experience and financial capacity of the borrower and contractor. Enter amount on line G.71 and in Section O of Form HUD-92264. Subject to Lender and HUD approval, the Borrower may elect to apply any funds remaining in the substantial rehabilitation construction contingency account after completion of the approved rehabilitation, to:

a. further improvements, betterments or upgrades to the property,

b. an initial deposit to the Reserve for Replacement account; or

c. reducing the mortgage balance.

If excess funds from contingency are used for betterments, those additional improvements will not be considered as the basis for a request for an increased mortgage amount.

2. Annual Deposit to Replacement Reserve. Because the rehabilitation work will result in a structure which will require no complete replacement of doors, windows, roofs, cabinets, or mechanical/conveyance systems for at least 5 years (see Chapter 5 Section 5.17), there is no initial deposit to the Reserve for Replacements for substantial rehabilitation. The cost analyst will work with the appraiser to determine the Annual Deposit to the Reserve for Replacement (ADRR). Monthly deposits to the Reserve for Replacement commence in accordance with the FHA Commitment. Calculations for the ADRR must be reviewed and appropriately revised every 10 years.

6.7 HUD Procedures for Pre-Application Stage

A. New Construction. No detailed cost estimate is done at the Pre-application stage. Cost estimation is limited to a review of the bottom line amount for Main Buildings on the borrower's application, Form HUD-92013. The HUD cost estimator will perform the review as follows:

1. The Lender will submit the Architect's sketch plans for the project.
2. Using the sketches, the cost analyst will determine the structure type and calculate the project's gross floor area.

3. Using construction cost data, the cost analyst will calculate an estimated Total Structures cost for the project's structure type and gross floor area.
4. The cost analyst:
   a. Will compare the estimated Total Structures cost with the borrower's amount for Main Buildings on Line 4 of Section G of Form HUD-92013, and will calculate a percentage difference between the two amounts;
   b. Will examine Total Land Improvements, General Requirements, Builder's Profit, Architectural Fees, Bond Premium, and Other Fees for reasonableness in comparison with established data.
   c. If the percentage difference is acceptable, accept the borrower's cost.
   d. If the percentage difference is in a questionable range, attempt to reconcile the percentage difference with the borrower to bring the borrower's figure into an acceptable range, or
   e. If the percentage difference is un-reconcilable, indicate in the review report that the project is infeasible.
   f. Prepare a review report (Appendix 6A.1) containing cost findings and submit to Team Leader.

B. Substantial rehabilitation.

1. Borrower's Cost Exhibits: Sketch plans and basic work write-up for rehabilitation work supplied by borrower's Architect as indicated in Chapter 5 Section 5.16, and borrower's summary cost estimate for proposed rehabilitation. Note that a bottom line estimate is only acceptable for complete substantial rehabilitation at this stage. For projects involving partial rehabilitation, the borrower's Architect must provide enough detail in the basic work write-up to establish a clear scope of work. The extent of rehabilitation work should be expressed in percentages. (Example: Remove and replace 20% of subfloor, 50% of kitchen cabinets, 25% of sinks and bathtubs, etc.). An itemized trade line item cost estimate is not required at this stage, but major trade groups, such as trowel trades (concrete, masonry), hammer trades (carpentry, drywall, insulation), and mechanical trades (plumbing, heating, electrical) should be separated.
2. HUD summary cost estimate of rehabilitation work: The cost estimator will do the following:
   a. Review the Lender's exhibits.
   b. Using available cost data, develop a summary cost estimate of rehabilitation work. The estimate will summarize rehabilitation costs for all main buildings, land improvement costs, and allowances and fees.
   c. Compare the HUD and borrower's cost estimates and report significant differences.
   d. Discuss differences with Lender in order to resolve.
   e. Prepare report (Appendix 6A.1) with recommendations:

      (1) If significant differences are resolved, accept the Lender's cost.

(2) If the differences are un-reconcilable, advise the Team Leader that the project is infeasible.

6.8 HUD Procedures for Firm Stage

A. Lender will submit:

1. Lender's completed cost package including the detailed cost estimate and the property insurance schedule.
2. Borrower's cost document package consisting of completed contractor's cost breakdown on Form HUD-2328, Contractor's and Borrower's Cost Breakdown, detailed plans and book specifications. For substantial rehabilitation, include useful life estimate of replacement reserve components (if applicable).

B. The HUD cost analyst will examine the Lender's cost estimate, the underwriting summary and the cost exhibits. The HUD analyst will review the quality of the Lender's estimate and the transaction itself. The HUD analyst will not reprocess the case. However, if the HUD analyst determines that certain underwriting conclusions are not supportable and affect HUD's risk, the analyst may recommend that the Lender modify the application or recommend a rejection. The Team Leader will approve, reject or modify the recommendation of the HUD cost analyst.

C. HUD cost analyst will review the Lender and borrower packages and will recommend either acceptance or rejection of the cost portion of the firm submission. Architectural exhibits, including construction documents, will be used as backup. HUD cost recommendations will be based on:

1. Comparison of Lender's estimate and contractor's HUD-2328 cost breakdown with HUD cost data. Comparison will include:
   a. Bottom line figures for total structures and land improvements and figures for allowances and fees;
   b. Cost Not Attributable;
   c. Examination of Lender-contractor variance report prepared by Lender's cost estimator, indicating resolution of cost differences.
2. Examination of identity of interest relationships and applications for identity of interest subcontractor overhead and profit.
3. Property insurance schedule.

D. HUD cost analyst will issue a written report (Format in Appendix 6A.2) containing recommendations and forward a copy to the HUD team leader.

E. Signatures. The Lender's cost analyst must sign and date Form HUD-2328 in the FHA: Processing Analyst box. The Lender's Underwriter must sign and date Form HUD-2328 in the FHA: (Chief, Cost Branch or Cost Analyst) box. The FHA (Chief Underwriter) line will be endorsed by both the HUD cost reviewer and the HUD Team Leader.

6.9 Section 223(f) - Lender Responsibilities and Deliverables

A. Responsibilities

1. The Lender prepares the Project Capital Needs Assessment (PCNA) and Replacement Reserve Escrow in accordance with Appendix 5G. The Lender's responsibilities are to:

   a. Prepare a Physical Inspection Report (PIR) containing an estimated cost, adjusted for inflation, to complete the projects:

      (1) Immediate repair needs; and

      (2) Expected repair, replacement, and major maintenance needs over a specified time period such as ten years.

   b. Prepare a Statement of Resources and Needs which:

      (1) Identifies:

         (a) All critical repairs which must be completed before initial/final endorsement and the associated cost of doing the work.

         (b) Non-critical repairs to be completed after final endorsement and the associated cost to be escrowed.

      (2) Recommends:

         (a) The amount of:

            (i) The initial deposit to the replacement reserve, if any;

            (ii) The monthly deposit to the replacement reserve.

2. The Lender's cost analyst's responsibilities are to:

   a. Complete the cost portions of Form HUD-92264, Project Income Analysis and Appraisal, regarding "as new" replacement cost. *

      * NOTE: The Lender's appraiser must work with the cost analyst to determine the "as new" replacement cost estimate and will enter the figures in Section G, lines G.36 through G.50 of Form HUD-92264.

   b. Prepare Form HUD-92329, Property Insurance Schedule. Note that Form HUD-92447, Property Insurance Requirements, will be prepared by HUD and provided to the Lender at closing. (See MAP Forms Book).

B. Deliverables at Firm Stage

1. Project Capital Needs Assessment containing estimates of critical and non-critical repair costs and the initial and monthly deposits to the replacement reserve.

2. Complete the cost portions of Form HUD-92264, Project Income Analysis and Appraisal, regarding "as new" replacement cost.

   NOTE: The Lender's appraiser must work with the cost analyst to determine the "as new" replacement cost estimate and will enter the figures in Section G, lines G.36 through G.50 of Form HUD-92264.

3. Independent Lender review of repair costs in PCNA.
4. Preparation of Form HUD-92329, Property Insurance Schedule. Note that Form HUD-92447, Property Insurance Requirements, will be prepared by HUD and provided to the Lender at closing. (See MAP Forms Book).

6.10 Lender Project Processing – Firm Stage

The Lender's cost estimator will prepare all required reports and recommendations indicated below:

A. Forms to Use
   1. Form HUD-92264
      a. Section G, Estimated Replacement Cost, Lines 36 through 50. Replacement cost figures are determined by the Lender's cost analyst and appraiser and entered by the Lender's appraiser.
      b. Section O, Remarks. When the Lender review of the PCNA is complete, the Lender's cost analyst will record totals for Project Repair costs and Initial Deposit to Replacement Reserve taken from the PCNA.
   2. Form HUD-92329, Property Insurance Schedule, used to determine the Maximum Insurable Value for all project structure based on Lender's appraiser's estimate of value after repairs.

B. There is no Cost Not Attributable for projects insured pursuant to Section 223(f).

C. Property Insurance Schedule, Form HUD-92329, provides a guide for the amount of insurance coverage. See MAP Forms Book for preparation instructions.
   1. Prepare form at submission of Firm Commitment package.
   2. Using estimate of value after repairs supplied by the Lender's appraiser, estimate 100% insurable value for each building.
      a. Value is of structures only. It does not include land value.
      b. Do not include the cost of land improvements, onsite demolition, or offsite work.
      c. Include the cost of major mechanical equipment, such as boilers serving the entire project, in the cost of the building where the mechanical equipment is located.

6.11 HUD Procedures for Firm Stage

A. Lender will submit a completed cost package including:

1. Cost estimates for repairs and Replacement Reserve deposits contained in the PCNA (prepared by Lender's Needs Assessor);
2. Independent Lender cost review of PCNA;
3. Summary Replacement Cost Estimate;
4. Property Insurance Schedule.

B. HUD cost analyst will review Lender exhibits and will recommend either acceptance or rejection of the Cost portion of the Firm submission. HUD cost recommendations will be based on review of:

1. Repair estimate based on the PCNA and compared with HUD data.
2. Lender's estimate for Initial Deposit to Replacement Reserve contained in the PCNA and compared with HUD data.
3. Property Insurance Schedule.
4. Any information produced by the Lender's architectural analyst which may affect cost.

C. HUD Cost Analyst will issue a written report (Format in Appendix 6-A) containing recommendations and forward a copy to the HUD Team Leader.

Chapter 7
Valuation Analysis & Market Study Requirements

7.1 Purpose of the Valuation Analysis

A. The Valuation Analysis evaluates the existing or proposed project as security for a long-term mortgage. Depending on program requirements, this includes an estimation of the market value of the property and an analysis of the market need, location, earning capacity, operating expenses, and warranted cost of the property.

B. The Valuation Analysis develops conclusions with respect to feasibility, suitability of improvements, extent, quality, and duration of earning capacity and other factors that have a bearing on the economic soundness of the property. The objective of the appraisal is to establish value for use in underwriting the supportable loan amount and to determine if the project will meet the market demand at rents that will pay operating expenses, reserves and debt service.

7.2 Selection of Appraisers and Market Analysts

The Lender is responsible for the selection and approval of appraisers and market analysts who are familiar with MAP guidelines. Lenders must ensure that each appraiser and market analyst selected is qualified to appraise or perform market analyses for multifamily properties by reviewing their education, quality, and frequency of multifamily appraisal experience, sample appraisals and market studies, professional affiliations, and state licenses or certifications. The ability to complete various HUD forms related to the appraisal, i.e. HUD-92264, 92273, 92274 etc., is also a requirement. The Lender may assist the appraiser in the preparation of these forms, and the appraiser must sign them unless he/she is not in agreement with value conclusions contained on the forms, in which case the Lender may prepare the HUD 92264-A.

A. Should the Lender have difficulty finding a Certified General Appraiser, the Appraisal Subcommittee of the Federal Financial Institutions Examination Council maintains a national registry of Certified General Appraisers who are authorized, under Federal law, to perform appraisals in connection with federally related transactions. The Lender may review this list at http://www.asc.gov, although inclusion on this list is not an indication of competency to perform multifamily appraisals.

B. The appraiser or the market analyst must be independent of and may not be affiliated with the loan originator, broker, developer, borrower, MAP Lender or any individual or institution involved in any other financial role in the application. The underwriter shall not act as the appraiser or market analyst.

C. The appraisal must be ordered and paid for by the Lender and not by the originator, broker, developer or borrower. The appraisal must identify HUD as an authorized user of the report. Appraisals

prepared by an affiliate, or not engaged or paid for by the Lender, are not acceptable and will not meet HUD's appraisal requirements.

D. The market study should be ordered and paid for by the Lender. However, a market study that has been prepared for the borrower by a third party market analyst and meets all other market study requirements of the Guide, including timeliness, is acceptable. The Lender is responsible for the review of all market studies submitted with the application.

E. In the selection of an appraiser or market analyst, there shall be no discrimination on the basis of race, color, national origin, religion, sex, age, or disability.

F. HUD Headquarters' reserves the right to examine the credentials of all appraisers and market analysts hired by the Lender, and to reject any individuals that it considers unqualified. HUD staff with concerns about a third party's capability, competence or experience should contact LQMD.

G. The appraiser Certification required by Uniform Standards of Professional Appraisal Practice (USPAP) must include a statement that the racial/ethnic composition of the neighborhood surrounding the property in no way affected the appraisal determination.

7.3 Appraiser and Market Analyst Qualifications

A. Each appraiser must meet the following minimum qualification requirements:

1. Be a Certified General Appraiser under the appraiser certification requirements of the state in which the subject property is located;
2. Be currently active and regularly engaged in the appraisal of multifamily properties;
3. Meet all requirements of the Competency Rule described in USPAP, which applies to each certified appraiser who signs the report. If any of the persons involved in preparing the report is a trainee acting as an assistant, this must be disclosed in the report;
4. Have at least three years of income property appraisal experience;
5. Be knowledgeable concerning current real estate market conditions and financing trends in the geographic market area where the subject property is located, and
6. Be experienced in appraising multifamily properties with the complexity and characteristics similar to those of the subject property. If the subject contains commercial space, LIHTC or other subsidies, the appraiser must have acceptable prior experience in the appraisal of comparable properties.

These requirements apply to each Certified General Appraiser signing the report. It is not permissible for an appraiser who is not certified in the appropriate jurisdiction to circumvent certification requirements by having a locally certified appraiser co-sign the report. Appraisers who are not certified in the appropriate jurisdiction may not perform the required property inspections of the subject or comparable properties. If any of the persons involved in preparing the report are not certified general appraisers and are acting as an analyst, assistant or trainee, this must be disclosed.

B. Temporary Certification. Temporary certifications are permissible; however, the above competency requirements still apply. The appraiser is responsible for checking the accuracy of all

information obtained from local sources and must indicate the names of all individuals who provided material assistance in preparing the appraisal. A temporary certification must be obtained prior to beginning the assignment. The Hub/PC may approve appraisers who have temporary certification who have documented how they will achieve competence in the subject's market area in accordance with USPAP.

C. Each Market Analyst must meet the following minimum qualification requirements:

1. Have at least 3 years of experience in performing market analysis for income producing property,
2. Be currently active and regularly engaged in performing market studies for multifamily properties,
3. Be knowledgeable concerning real estate market conditions and financing trends in the geographic market area where the property is located, and
4. Be experienced in performing market studies for multifamily properties with the complexity and characteristics similar to those of the subject property. If the subject contains commercial space, LIHTC or other subsidies, the market analyst must have acceptable prior experience in the market of comparable properties.

D. If the Hub/PC believes that a Lender is contracting unqualified or unlicensed appraisers or market analysts, the PC must refer the case to LQMD for investigation.

7.4 Market Study Applicability and Requirements

A. Applicability. For all new construction properties and all substantial rehabilitation projects with significant resident displacement, resulting in negative cash flow during the rehabilitation period and for all LIHTC transactions without project based rental assistance, the appraisal and market study should be completed by different firms. The Hub Director can waive this requirement on a case-by-case basis, if it is clear the appraiser or appraisal firm is capable of performing both the subject appraisal and the macro market analysis, and if the strength of the market is not in question. Section 223(f) proposals typically do not require a market study separate from that contained in the appraisal, however, in volatile or declining markets, the Lender should consider, and may be required to obtain, such a market study to support the underwriting conclusions of market demand for the subject property over the loan term. Market studies are not required for properties with at least 90% of the units covered by a long term (5 years or more) rental assistance contract and with any rent increase confirmed before initial or final endorsement.

B. Requirements. Each market study must meet the following requirements:

1. Meet the requirements of Section 7.2B and D.
2. Meet the content and format requirements of Section 7.5.
3. Effective Date. For pre-applications, the effective date of the study must be within 120 days before the date of the pre-application package. For Firm Commitments, the effective date of the study must be within 180 days prior to the issuance, re-issuance or amendment of the Firm Commitment. Expired reports must be updated as needed by re-surveying all relevant data.

4. Have the information from the Lender listed in Appendix 4.
5. Be prepared in conformance with the market study format in Section 7.5.
6. In cases where a waiver is granted and the appraiser prepares the market study, it must be submitted as an independent exhibit and separately bound report.
7. Include the market analyst's certification per the format in Chapter 11.

7.5 Content and Format of the Market Study

A. Purpose and focus of the study. The purpose of the market study is to assure that there is enough sustainable demand for additional units without adversely impacting the existing supply, so as to maintain a balanced overall market. The focus of the market study is on the overall demand within a defined market area, and of the proposed project's ability to capture and sustain a share of the total or incremental demand. The market study is typically narrow in its geographic coverage than the market analysis prepared by EMAD, which analyses the broader MSA. The study must estimate the number of renter households with sufficient incomes to afford the type of housing at the rents proposed. In addition, the study must estimate the number of units that the market could reasonably absorb over a specified forecast period, which is typically three years, taking into consideration competitive units in the existing inventory, units currently under construction, and units in the planning pipeline, as well as the gross and contract rents of those units.

For projects designed for the elderly, age 62 and over, the study must estimate the number of elderly households with sufficient incomes to afford the type of housing and services under study, the proportion of those households that would need and demand such housing, and the number of units that the market could reasonably absorb and sustain over the forecast period. Useful information may be obtained from the Form HUD-92013, "Supplemental Application and Processing Form Housing for the Elderly/Disabled."

B. Executive Summary. All market studies must contain an Executive Summary with a concise summary of the data, analyses and conclusions, including the following:

1. a description of the site and the immediate surrounding area;

2. a summary of the project, including the proposed targeted population;

3. a statement of key conclusions reached by the analyst;

4. a statement of the analyst's opinion of market feasibility, as determined by factors of market demand;

5. recommendations and/or suggested modifications to the proposed project, if appropriate;

6. a summary of competitive advantages and disadvantages, and issues that will affect the property's marketability, performance and lease-up, as well as points that will mitigate or

reduce any negative attributes.

C. Description of the proposed project. The market study must include a thorough description of the proposed project, including:

1. The number of units by type and size with information on the number of bedrooms and bathrooms, structure type, square footage, etc. Actual (paint to paint) size should be noted as well as the size in published brochures or other media.

2. The proposed market rents and gross rents by unit type. (Gross rent is defined as the cost of renting the unit, including the cost of resident paid utilities.)

3. The unit and project amenities and services.

4. The project location in terms of:

   a. Characteristics of the neighborhood in relation to schools, transportation, shopping, employment centers, social and community services, etc., to include a study of the adequacy of the public facilities that will service the site. The report must include a map showing the site and important neighborhood facilities and amenities.
   b. Any other locational considerations relevant to the market and marketability of the proposed project.

5. Description of income or rent restrictions imposed on the project by the use of public financing and/or subsidies (e.g., LIHTC, tax-exempt bonds or subordinate loans).

   The report must address, in sections E. and G., how these incomes and rent restrictions will affect potential demand, absorption and long term stabilized occupancy of the income-restricted units.

6. Characteristics of the proposal that will have a specific bearing on its market prospects and overall marketability, such as location, amenities, features or design.

   a. For projects designed for the elderly, age 62 and over: The estimated total monthly fees for shelter and any separate fees charged for any optional services per resident by type of occupancy or accommodation.
   b. The estimated total monthly fees for any optional services provided on an as needed per resident basis.
   c. The proportions of the project to be occupied by market rate residents and by public pay/assisted residents-tenants, e.g. Optional State Supplement.
   d. The amenities and special services to be provided and how they support the physical, mental, or social conditions of the prospective residents.
   e. The project location and its proximity to facilities and services essential to elderly

residents such as hospitals, medical/health care facilities, social and community services, public transportation, shopping and recreational activities; and any other locational considerations relevant to the market or marketability of the proposed project. Include a map showing the site and important facilities and services.

D. Housing Market Area (HMA) is the geographic area in which units with similar characteristics, e.g., number of bedrooms and rents, are in equal competition. The location of the competing projects and where the majority of the residents will come from must be discussed. The size of the HMA for general occupancy rental housing can vary significantly depending on the extent and location of comparable and competitive products within a specific area. In some cases, both a primary and secondary market area must be defined. When defining the boundary of a market area, the analyst should consider the locations of comparable and competitive rental developments (existing, under construction and developments in planning) and commuting times from employment. Data on place of work or residence, population from the 2000 to 2010 (once available) Decennial Census, American Community Survey (ACS) and local sources will aid in this determination. The market study must include the following:

1. A map of the HMA, showing delineated boundaries, location of the subject, major highways and thoroughfares, geographic features like rivers and lakes, and political divisions such as state lines and city limits. The map must have a title, bar scale, north arrow and legend.

2. A description of the geographic boundaries of the HMA and a justification for the delineation, including a discussion of the location of competitive housing, relevant services and amenities and concentrations of employment opportunities.

3. A description of the sub-market for the type of housing proposed, defining the economic and demographic characteristics of the target market in terms of income levels, household size and age range of prospective residents.

4. A statement of the length of the specified forecast period, which is typically 36-48 months from the current date of the study.

5. For projects designed for the elderly, age 62 and over:

    a. the locations of the prior residences of the current occupants in comparable and competitive existing projects,

    b. location and access to relevant services and amenities,

    c. any concentrations of elderly population,

    d. a description of the sub-market for the type of housing and care proposed by the economic and demographic characteristics of the target market (projected residents): income levels, wealth and assets, household size, age of prospective residents, physical and/or mental limitations, homeownership rates, and other similar factors,

e. description of the current inventory foreclosures and defaults, quantitative and qualitative characteristics of projects in the market area, occupancy rates and waiting lists,

f. total monthly charges by unit type, including the monetary level of concessions, type of accommodation, and level of services,

g. typical types of services and amenities offered, whether mandatory or optional fee for services, and whether services are provided by the facility (directly or by contract) or through a third-party arrangement (tenant-resident and provider and any added costs for optional services), and

h. absorption experience of recently completed projects on a units per month basis, discussing the level and extent of pre-sale or pre-marketing efforts.

6. For LIHTC Projects. Provide an estimate of demand, including a capture rate, based on potential income eligible residents. An income eligible resident is a resident whose income does not exceed the maximum permitted by the affordability restrictions but who has sufficient minimum income to pay the LIHTC rent without being overburdened. To make these determinations, consider the following information and guidance:

   a. When the proposed rents are set at the LIHTC maximums, the market of income qualified residents for the restricted units is comprised of a relatively narrow band of income eligible renters whose incomes do not exceed the maximum but are sufficiently high to pay the rent without being overburdened, which can result in a problem with the market feasibility of the project. Depending on the rental market and income conditions in the HMA, there may be an insufficient number of potential renters that meet the income limit and who are also able to pay the restricted rent. In many markets, LIHTC projects set their rents below the maximum permitted. Some LIHTC projects have other forms of assistance (such as Section 8 rental assistance or soft subordinate financing) to further reduce rents and thus expand the number of income eligible residents.

   b. The determination of demand and the capture rate should take into consideration:

      (1) the current and anticipated supply/demand conditions in the overall rental market,

      (2) the potential depth of the market of income eligible households in comparison to the number of units at the proposed rents, and

      (3) the marketability of the proposed units taking into account the project's amenities, rents and location relative to comparable and competitive projects and other available housing options.

   c. Capture Rate is defined as the percentage of households in the HMA that meet any

applicable age and household size restrictions and are within any limited income eligible band and who have sufficient minimum income to pay the tax credit rent without being rent overburdened, who the property must capture to fill the units and achieve stabilized occupancy. The Capture Rate is calculated by dividing the total number of units at the property by the total number of households that meet the applicable age, size and any income band requirements. The absorption rate is defined as a projection of the pace of unit lease up as units become available for occupancy.

The Hub/PC should consult with EMAD in assessing the determination of eligible income band, capture rate and absorption rate contained in the market study. If the Hub/PC finds that there is insufficient demand for the units at the proposed rents, the loan should be either rejected or revised by the Lender with rents lowered as necessary to broaden the band sufficiently to ensure adequate absorption and achieve stabilized occupancy. If agreement cannot be reached with the borrower on the appropriate rent levels, the project should be deemed to be not feasible and rejected.

E. General characteristics of the HMA. The market study must include a thorough description of the current and forecast economic and demographic characteristics and conditions of the HMA. The description is necessary to provide background and justification for the subsequent estimates of demand for additional rental housing. The study must include the following:

1. A discussion of current economic conditions and employment characteristics, including:

   a. Identification of growth sectors in the economy and emerging trends, including a detailed discussion of the sectors in the economy that have a major impact on the local housing market, such as military facilities, colleges and universities, federal and state government, major employers or tourism.

   b. A study of recent trends in employment, including unemployment statistics and new job creation or loss, with a detailed discussion of:

      (1) Any anticipated changes in employment as a result of expected closings, openings, expansions or cutbacks by leading employers, with a particular emphasis on how this would affect the rental market during the forecast period, including any seasonal employment markets.

      (2) Information on the types of new jobs being created and lost, including data on pay scales and how these wage levels relate to the affordability of the proposed rental units.

      (3) List of major employers in the HMA, the type of businesses and the number employed.

      (4) In relevant markets (such as resort areas), comment on the availability of affordable housing for employees of businesses and industries that draw from the HMA.

c. A forecast of employment for the specified forecast period and how this forecast supports demand for additional new rental housing.

2. A thorough discussion of past and anticipated future trends in the demographic character of the housing market, covering such subjects as population change, migration, net natural change, household growth or decline, changes in the average household size and changes in tenure. The report must include estimates of the total population and households (by tenure - owners and renters) that include the current date of the study and the forecast date (three or four years from the date of the study) and a detailed explanation of all significant trends and changes.

3. Income Restricted Projects. Provide a discussion of other income–restricted projects that are existing are under development or are proposed in the HMA, while keeping in mind the eligible income band. Particular attention must be given to existing, under construction and proposed projects that would require an eligible income band that is similar to the subject's.

F. Current housing market conditions. The market study must include a comprehensive description of the current conditions of the rental market and of the sales market, if relevant, in the HMA. This description should include a summary statement on the current condition of the overall rental market and of the rent levels in the market of comparable projects, including the following:

1. An estimate of the current competitive rental inventory, of both single-family and multifamily units, in the HMA, with data on the number of units by structure type, by number of bedrooms, by rent levels, age and location.

2. A thorough discussion of recent market experience analyzing the following:

a. Current occupancy levels and recent trends in occupancy/vacancy in existing rental projects.

b. Absorption experience of recently completed rental developments, including estimates at a project level of per unit per month absorption rates, with particular emphasis on comparable and competitive projects that have entered the market within the past 24 months. When available, annual absorption of new projects from the past 10 years should be provided.

c. Current gross rents for comparable and competitive projects, and the trend in rent increases in this inventory during the past 24 to 36 months. The description should identify any services included in base rents or offered at a premium. Where relevant, the report should include information on the extent of rent concessions or similar incentives, particularly in projects in initial occupancy and must address the impact of concessions on rent levels and whether the quoted rents are overstated due to concessions or other factors.

d. Estimated current overall rental vacancy rate and vacancy rate for units similar to those in the proposed project. Significant seasonal variations in vacancy rates, if applicable,

should be discussed.

e. Discussion of any vacancy or absorption problems in the market, particularly in the segments of the market most relevant to the subject project, including the cause if the subject's rates are significantly higher or lower than the overall rental vacancy rate.

f. The impact, if any, of the single family and condominium market conditions, including an analysis of the cost to rent versus to own, and the impact of foreclosures and of the shadow single family and condominium rental market.

3. The report must include a map showing locations of existing competing rental projects, projects currently under construction, and those in the planning and development process.

G. Characteristics of Rental Units in the Pipeline, Under Construction and in Planning. The market study must include separate estimates of the numbers of rental units currently under construction and the numbers in the planning and development process likely to enter the housing market during the specified forecast period. These estimates should include all rental developments known, not solely those determined by the analyst to be comparable and competitive. The description of the pipeline activity should clearly identify any significant characteristics of specific developments with rent restrictions or rent limits such as LIHTC or age-restricted occupancy. The report should contain estimates of:

1. The number of projects currently under construction, the total number of units, the numbers by bedroom size (number of bedrooms) by rent range, structure type and their locations.

2. The number of projects in planning stages that are likely to be developed, including but not limited to those with building permits or firm financial commitments, including details on the number of units by bedroom size, rents, locations, and stage of development.

3. A list of LIHTC projects in or near the market area that are not yet placed in service, giving as much known detail as possible on estimated placed-in-service dates, unit mix and income levels to be served.

4. For projects designed for the elderly, age 62 and over:

a. Total monthly charges by unit type, type of accommodation, and level of services, with information on the added costs for optional services.

b. Typical types of services and amenities offered, whether these are mandatory or optional fee for services, and whether services are provided by the facility (directly or by contract) or through a third-party arrangement (resident and care provider).

H. Demand Estimate and Study. The market study must include an estimate of future demand for the specified forecast period, typically 36 to 48 months. The estimate of demand and the study supporting that estimate must meet the following guidelines:

1. The estimate of demand must be based on a calculation of incremental demand and must address the following factors:

    a. Renter household growth during the forecast period.

    b. Recent trends in tenure broken down by homeownership and rental that may increase/decrease the demand for rental units.

    c. Replacement of existing rentals lost from the inventory due to demolition, conversion, shifting owner units into the rental market and by other means, and consideration of any current excess vacant supply based on a balanced market vacancy rate. The demand estimate must reflect the number of rental units that, if added to the inventory, would promote balanced market conditions.

2. The estimate of demand should be broken down into a qualitative estimate of demand by number of units by bedroom size, rent range, and other relevant characteristics, as necessary.

3. The demand estimate should identify the "effective demand" pool of households with sufficient incomes and or applicable household size that would be expected to demand such housing during the forecast period, including the income levels and rent- to-income ratio(s) assumed in the study.

4. The study must reconcile the number of units in the proposed project with the demand estimate for the HMA, taking into consideration current housing market conditions, available vacancy, and forecast additions to the supply (under construction and in the pipeline). The study should also include an estimate of the absorption period needed for the project to reach sustaining occupancy based on current market data and the *quantitative and qualitative demand* estimates.

5. The market study must include an assessment of the impact the proposed project would have on existing rental developments. Specifically, the study must address the impact on existing insured properties and show that demand will come from new renter households, the shifting of households into the rental market, or the replacement of lost or sub-standard units. It must be demonstrated quantitatively that the number of units under construction and the proposed supply, including the subject, will not create over-supplied or overall soft market conditions. Even if the subject does not directly compete with existing insured or uninsured properties, an oversupply of units could spill over into all segments of the market.

6. For projects designed for the elderly, age 62 and over:

    a. The demand estimate should reflect "effective demand" and should be based on the numbers of elderly households meeting the relevant economic and demographic criteria (sufficient incomes, age, household size, and need for the type of shelter and care) that reasonably could be expected to demand such housing during the forecast period.

b. The report must include a descriptive study of the demand estimate that addresses the primary determinants including:

(1) Current and forecast population and households of the target group(s) by age cohort and the proportion of the market each group comprises.

(2) Current income level/band of income of prospective households comprising demand, including cost/rent to income ratio(s) assumed in the study.

(3) Changes in the population (including migration patterns) of adult children of the potential elderly occupants. Discuss the impact of anticipated population changes on the demand for the project and the portion of demand expected to come from outside of the primary market area.

7. For Income Restricted Projects. Discuss demand and calculate the capture rate based on the eligible income band considering the proposed project's income restricted unit mix and restricted rents. In calculating the capture rate it is important to confirm that the income qualified renter households in the HMA used in the determination have an eligible income band similar to the subject.

I. Additional Requirements for Projects designed for the elderly, age 62 and over Basic Assumptions of the Study. The technical and analytical methods used by the market analyst and all conclusions must be consistent with the following assumptions:

1. There is a direct relationship between the housing and needs or requirements of an elderly person and the limitations in activities of daily living imposed by the physiological, psychological, and social changes of the elderly. Therefore demand and need vary between different age-cohorts of elderly for particular types of housing.

2. The demand within each age-cohort for a particular type of product will depend on the housing and services offered and how well these meet the physical, mental and social conditions and service or care needs of persons within each age-cohort.

3. In addition to their normal source of income (pensions, social security, and retirement funds) the elderly demanding shelter and care will use some portion of their assets (net worth) to defray the cost of shelter and care. Elderly homeowners may sell their homes and use part of the investment income from the net equity toward the monthly housing expenses.

4. The proportion of income an elderly household is willing to pay for a particular housing product (cost-to-income ratio) will depend on the type and extent of services included in the total monthly cost. The more extensive the level of shelter and services the higher the ratio. The cost to income ratio is defined as the sum of the shelter rent, utilities, and typical service charges, divided by the total monthly household income. Cost to income ratios are a function of the type of housing product and the level of services and amenities provided. The cost to income ratio used in the study should also reflect what is reasonable and customary for the particular type of housing in the subject market area, taking into consideration recent market

experience of comparable and competitive product. A guideline for cost-to-income ratios for age-restricted rental apartments with no services should be 30 percent or less.

5. One-person households comprise the major segment of the demand for housing and supportive services for the elderly. Therefore, any estimates of demand based on data for the total elderly population or for all elderly households, must be adjusted to be consistent with actual market experience and occupancy by household size in existing competitive product.

6. Household Sizes and Counts. Use of data on all household sizes must be adjusted to derive an accurate demand estimate, consistent with the characteristics of the target market. If an analyst makes an estimate of demand using data for all households, without making an adjustment for household size, the subsequent estimate of potential demand will be significantly overstated.

7. Using counts for total households substantially overstates the number of income affordable households. Census data indicates that incomes of two-person households are approximately twice that of respective one-person households. Consequently any distribution of elderly households will have a greater proportion of two-person households in the upper income ranges than one-person households. Analyses shows that at most every income level, two-person households typically out-number one-person households by a factor of two or three to one, depending on age.

8. Unless a factor is applied to the "all household" count to adjust for this bias the demand estimate is incorrect. The method most analytically consistent with the observed facts of the target market for most seniors housing would be to measure the numbers of elderly one-person households, with incomes sufficient to afford the type of housing, and then adjust this count to take into account households of other sizes.

J. Additional Requirements/Guidance for Income Restricted Projects. According to USPAP Advisory Opinion 14:

"Subsidized housing may be defined as single- or multifamily residential real estate targeted for ownership or occupancy by low- or moderate-income households as a result of public programs and other financial tools that assist or subsidize the developer, purchaser, or resident in exchange for restrictions on use and occupancy." While HUD provides the primary definition of income and asset eligibility standards for low- and moderate-income households, other federal, state and local agencies define income eligibility standards for specific programs and developments under their jurisdictions.

The competency required of appraisers and market analysts to appraise or prepare market studies on subsidized housing extends beyond typical multifamily residential experience and requires an understanding of the various programs and definitions involved in the particular subsidy program applicable to the development. Practitioners should be capable of analyzing the impact of the programs in the local subsidized housing submarket, as well as in the general market that is unaffected by subsidized housing programs, and must be aware of possible political changes that will affect the continued availability of the subsidies and must fully understand the requirements

for subsidy programs. A lack of knowledge and understanding of the impact of the unique influences that affect subsidized housing projects could lead to misleading conclusions.

K. Data, Estimates, and Forecast. The study should document the methods and techniques used to develop all estimates and forecasts and provide adequate citations on the sources of all data, estimates and forecasts which citations must be relevant and current. Conclusions in the study must be consistent with the facts presented; findings and recommendations should be based on a reasonable forecast of market supply/demand conditions and sound assumptions regarding capture rates, absorption, achievable rents, income affordability and similar factors. To the extent possible, the qualitative and quantitative estimates of demand for additional rental units should take into account the changes in renter households by household size, not just in total. Although data for all household sizes may be used, a study of the trend of change by household size may derive a more representative and accurate demand estimate consistent with the characteristics of the target market.

L. Useful Information. Distributions of total renter households by size of household (1, 2, 3, 4 or more persons), or by age of householder (15 to 61, 62 to 74, or 75 and older) by income intervals are readily available from the HUDUSER website, http://www.huduser.org/ datasets/spectabs.html.

7.6 Appraisal Requirements

A. Each appraisal must meet the following requirements:

1. Each appraisal shall be presented as a Self-Contained Report prepared in accordance with USPAP Standards Rule 2. The development of the appraisal must comply with USPAP Standards Rule 1, and the Scope of Work Rule and assignment conditions outlined throughout this guidebook. The report should contain all of the information necessary for loan underwriting and for the HUD review appraiser to easily understand the reasoning employed by the appraiser.

2. Complex or Unusual Appraisal Assignments. Experience has shown that changes in the cost and manner of constructing and marketing commercial, industrial, and residential real estate as well as changes in the legal framework in which real property rights and interests are created, conveyed, and mortgaged result in corresponding changes in appraisal theory and practice. The appraisal profession is constantly reviewing and revising appraisal methodology to meet these changes. When an appraisal assignment involves a subject with property rights issues or other unusual circumstances, third party appraisers must be sure to compliance with USPAP Standards Rule 1-1(a), "In developing a real property appraisal, an appraiser must be aware of, understand, and correctly employ those recognized methods and techniques that are necessary to produce a credible appraisal."

   When an appraisal or consulting assignment involves complex or unusual valuation issues, the appraiser and the Lender should consult with the Hub/PC before beginning the assignment.

3. Form HUD-92264 and supporting forms HUD-92273, HUD-92274, and HUD-92264T (if applicable) must also be prepared and included in the report along with a copy of the Lender's

HUD-92264-A, or a draft completed by the appraiser. The appraisal report must be supportive of and consistent with the conclusions made on the forms.

4. The USPAP Jurisdictional Exception rule is not generally applicable in HUD appraisal assignments. Limitations on occupancy rates and commercial income/space, etc., imposed by the insurance programs are considered to be conditions of the assignment.

5. Occupancy Percentage. Occupancy Percentage. The estimate of occupancy for residential properties should be based on the occupancy that is prevalent for the subject's area, without regard to FHA programmatic constraints imposed on the maximum underwritten occupancy when calculating debt service coverage. The estimate of occupancy should take into account the historical performance of the subject and the vacancy and collection loss typical for the subject's market area. The estimate should ignore unsustainable market conditions, short-term spikes in the occupancy rate due to reasons such as seasonal changes and short-term demand for specialized employment, i.e. disaster relief workers.

6. Sections 220, 221(d), and 231 (new construction only) do not call for an "as complete" value conclusion. The valuation for these programs is considered an Appraisal Consulting Assignment subject to the development and reporting requirements outlined in Standards 4 and 5. However, the appraiser must ensure that any opinion of value that is used in the consulting assignment was developed in accordance with Standard 1.

   a. These are replacement cost limited mortgages by mandate of the National Housing Act and require a site valuation, a debt service analysis and a cost approach to value. An estimate of the market value after completion is not required. The appraiser must fully examine the proposed construction costs of the subject property. Plans, specifications and development costs must be presented, analyzed and supported by the cost approach using either a subscription cost service such as Marshall & Swift, the Lender's cost analyst or a direct comparative analysis of recently completed similar developments. Substantial Rehabilitation projects require an estimate of the "As Is" value of the property by use of the income and direct sales comparison approaches to value when possible. Unoccupied or "shell" structures may be appraised using the sales comparison approach only.

   b. According to the USPAP, "Standard 5 does not dictate the form, format, or style of real property appraisal consulting reports. The form, format, and style of the report are functions of the needs of users and appraisers. The substantive content of a report determines its compliance." Therefore, the appraiser and the MAP underwriter must assure that there is sufficient narration and exhibits to allow a reliable underwriting decision to be reached. This should include, but is not limited to, location maps, photographs of the subject, rent and expense comparables, site and floor plans, along with thorough explanations of all adjustments.

7. For Section 223(f), all three approaches to value must be utilized for subjects that have an actual age of less than ten years. When there are repairs or allowable improvements proposed,

these appraisals must be prepared assuming those repairs/improvements have been completed and rents and expenses must reflect completion of the proposed repairs or improvements.

a. Cost/ Summation Approach. The cost or summation approach must consider all applicable forms of depreciation, functional and external obsolescence. For this reason, the cost/summation approach shall not automatically set the upper limit of value for these programs. However, this policy is not intended to negate the necessity of the final reconciliation of the three approaches but is rather an acknowledgment of the basic principle of substitution in that no prudent purchaser would pay more for a property than the cost to acquire a similar site and construct improvements of equal desirability and utility. This approach may be eliminated at the discretion of the appraiser, for subjects that are ten or more years old.

b. Sales Comparison Approach. In multifamily housing, the entire project typically does not offer a convenient basis for comparison with other entire projects due to differences in size, composition, areas, units and rooms. Acceptable units of comparison are price per living unit, price per room, price per square foot of gross building area (GBA) and gross rent multiplier (GRM).

c. Income Approach. The annual net operating income (NOI) remaining after the payment of expenses is considered to be the primary source of value to the property. The preferred method of capitalizing the NOI into a value estimate is Direct Capitalization. There are several acceptable techniques for deriving capitalization rates. Rate Extraction based on recent (preferably within the past year) comparable sales is the most preferred. Band of Investment, Ellwood, and Sinking Fund, etc. are also acceptable. The appraisal should also contain discussion of how the chosen capitalization rate compares to rates listed in published reports such as Korpacz, realtyrates.com, etc. The Department does not recognize the use of Discounted Cash Flow Analysis on appraisals for mortgage insurance.

   The Capitalization Rate must be based on factors reflecting the overall demands of knowledgeable investors in properties similar to the Subject. Regardless of the method used in deriving the rate; it must be supported by current market information, i.e. recent sales, typical loan terms and return on owner's equity. The appraiser must report all market comparables used to derive the Capitalization Rate.

8. For Section 231 Substantial Rehabilitation cases, follow the instructions for Section 223(f). Substantial rehabilitation under Section 231 differs from Sections 220, 221(d)(3) and 221(d)(4) in that a market value based on the completion of the rehabilitation is required.

9. Remaining Economic Life (REL). REL is defined as the estimated period during which improvements will continue to contribute to property value and an estimate of the number of years remaining in the economic life of the structure or structural components as of the date of the appraisal.

   a. For new construction and substantial rehabilitation projects, the maximum mortgage term is the lesser of 40 years, or 75 percent of the REL.

b. For existing properties, the maximum mortgage term is the lesser of 35 years, or 75 percent of the REL.

c. Estimation of the REL is first accomplished by determining the economic life of the improvements (as new) through market analysis and/or an appropriate reference source. The appraiser then reduces the economic life (as new) by the effective age to determine the estimated REL. For example: original economic life (say 55 years) is reduced by the effective age (say 15 years) = 40 years estimated REL. The effective age is determined by the appraiser based on the actual condition of the subject considering all applicable forms of depreciation, and after assuming the required repairs to be made as specified in the PCNA as a condition of refinancing. The REL is then multiplied by 75 percent to determine the maximum mortgage term as described above. In this example, the maximum allowable term for the mortgage would be 30 years (55 less 15 = 40 x .75 = 30 or the lesser of 35 years or 75% of REL (30). The methodology and reference/data sources used by the appraiser must be clearly set-forth in the report and must consider all of the following factors:

(1) The economic make-up of the community or region and the ongoing demand for accommodations of the type represented.

(2) The relationship between the property and the immediate environment. Older properties may have legally non-conforming use if they pre-dated real property zoning for the neighborhood. Observations within the neighborhood in which the subject is situated may reveal a conflicting relationship. This should be fully explored to determine any potential external obsolescence.

(3) To the extent possible, the appraiser should analyze architectural design, style and utility from a functional point of view and the likelihood of obsolescence attributable to new inventions, new materials, changes in building codes, and changes in tastes. The appraiser should indicate in the Scope of Work the steps taken to accomplish this requirement.

(4) The trend and rate of change in the characteristics of the neighborhood that affect property values and their effect on those values.

(5) Workmanship and durability of construction and the rapidity with which natural and man-made forces may cause physical deterioration.

(6) Physical condition and the practice of owners and occupants with respect to maintenance, the use or abuse to which the improvements are subjected, the physical deterioration and functional obsolescence within the subject property.

The REL directly impacts the amortization period and the maximum insurable mortgage. An over-estimate of the REL can lead to greater risk to the Department. An under-estimate can unfairly penalize a project. HUD review appraisers should carefully scrutinize the methodology used in estimating the REL.

10. HUD is the regulatory enforcement agency identified in the Confidentiality Rule of USPAP. Appraisers will be required to present their entire work file and fully disclose the identity and source of confidential information should the Department determine a review of the appraiser's work file is in order. (Note that, per USPAP, disclosure to enforcement agencies does not constitute a violation of the Confidentiality Rule.) Any irregularities noted during the appraisal review process may trigger a review of the appraiser's work file.

11. Effective Date. For pre-applications, all appraisals must have an effective date within 120 days before the date of the pre-application package. For Firm Commitments, all appraisals must have an effective date within 180 days prior to the issuance, re-issuance or amendment of the Firm Commitment. HUD defines the effective date as the most current date that the appraiser inspected the subject, comparables and made estimates of rents and expenses. Updated appraisals can be submitted if the appraiser re-inspects the subject property, re-surveys the rental comparables, and reviews the market for any additional sales comparables. Follow USPAP Advisory Opinion 3 for guidance on completing and reporting appraisal updates. Lenders should provide for updates in their response to the invitation letter in case of processing delays prior to issuance of the Firm Commitments.

12. The appraisal must be prepared with the list of information contained in Appendix 4.

13. Include an appraiser's Certification with the format in Chapter 11.

14. Inspection of the Subject and Comparables. The primary appraiser designated by the Lender and accepted by HUD must physically inspect the subject (both exterior and interior) and all of the comparables used as part of the analysis. The primary appraiser must also sign the Certification within the appraisal report and the supporting HUD forms.

    a. The primary appraiser must inspect at least one of each bedroom/unit type. The total number of units inspected must equal or exceed 5% of the total number of units for projects of up to 200-units, or 4% of the total number of units for projects greater than 200-units. If the characteristics and/or condition of the subject indicate that a higher level of inspection is necessary, it is the appraiser's responsibility to expand the scope of the work as is necessitated by the observations made by the primary appraiser during the inspection of the subject. This is especially important where the improvements are high-rise structures whereby individual units within demonstrate varying degrees of light and view qualities. If there are hazardous conditions or other factors that preclude a thorough inspection of the interior, the appraiser must clearly indicate these circumstances in the appraisal report.

    b. For large projects exceeding 500 units, the Lender may request a lesser percentage and reasonable number of units to be inspected by the appraiser. In addition, the appraiser may employ assistants to inspect individual units so as to encourage a thorough inspection. The names and qualifications of these assistants must be disclosed in the appraisal report. The assistants are not required to sign the report.

c. The primary appraiser must inspect all of the comparables used in deriving and estimate of value, including land comparables (if applicable), improved comparables sales, expense comparables and rental comparables. The appraiser must verify the condition of the comparables with management or other personnel familiar with the property whose contact information must be documented in the appraisal report.

15. Required Appraisal Report Exhibits. Photographs (subject, and all comparables including rentals), regional map, location map, satellite scans (if available from Google, Bing, etc.), flood hazard map, survey (if available), floor plans (for each type of unit being offered - if available), site plan, zoning map, tax map, land sales comparable map, rental comparable map, and improved sales comparable map are required with all submissions.

16. Market Analysis Requirements for Multifamily Appraisals. The appraisal must also contain, depending on the complexity of the project and prevailing market conditions, a Level B or C Market Analysis of the local market with an emphasis on multifamily housing so as to determine the ability of an existing property to continue usage as multifamily housing. In the case of proposed construction or substantial rehabilitation, the purpose is to determine overall feasibility and demand for new housing units. A brief outline of a Level C analysis follows:

    a. Location. This includes a general description, specific analyses of site linkages and urban growth determinants and detailed competitive location rating.

    b. Demand Analysis. This includes a discussion of general evidence of sales/leasing activity, general city/area growth trends, market absorption, demand and need forecast based on population, employment and income and a demand forecast of the subject market segment.

    c. Competitive Supply Analysis. This includes vacancy rates for comparables and from market surveys (secondary data), field research on all competitive and proposed properties, building permit analysis, identification of proposed sites, and a detailed competitive amenities rating.

    The detailed requirements for performing a Level B or C analysis can be found in “Market Analysis for Real Estate”, published by the Appraisal Institute. In general, a stable market evidenced by a recent sales, and balanced supply and demand is an indication that a lower level “B” analysis will be sufficient. If there is uncertainty in determining the level of analysis, the Lender and appraiser should jointly consult with the Hub or Program Center.

B. The certification required by USPAP must include a statement that the racial/ethnic composition of the neighborhood surrounding the property in no way affected the appraisal determination.

7.7 Estimating Project Income

A. Rental estimates. Estimate the annual gross income of the subject project including estimates of income from market comparables, rental concessions, and an assessment of the general health of the rental market. The gross income estimate assumes a full occupancy level and reflects rent levels current as of the appraisal date or date of the market study. Also, the effect that any proposed repairs to the project will have on rents, expenses, and net income must be considered, although not all repairs increase rents, occupancy, net income, and/or decrease expenses.

B. Rent comparables. Market rent by comparison shall be estimated by the appraiser and documented on the HUD-92273. Note that use of Form HUD-92273-S8 is not authorized for application processing.

1. A separate HUD-92273 is to be prepared for each type and size (if significantly different) of rental unit in the subject property.

2. The rent comparables and units selected for comparison must be as similar as possible to the subject property and units as to location, structural type, number of bedrooms, and average unit size. In order to ensure they are truly comparable and competitive with the subject property, appraisers should generally not use rent comparables located outside of the subject's market area unless there is a lack of recent comparables in the subject's immediate market area. In this case, the comparables selected should be from areas similar to the subject and this should be fully explained in the report.

3. Market rate units from partially assisted projects can be used as rental comparables in the absence of better rental data.

4. Consistent adjustments for significant differences between the comparables and the subject units shall be derived from the market and applied to the subject rent estimate. Rental adjustments are always made to the comparables for differences with the subject project.

5. The appraiser should select the final rent estimate based on accepted correlation procedures:

   a. Generally, the indicated rent estimate will be from the central 60% of the rental range of the indicated rents after proper adjustment. In situations where the appraiser gives the greatest weight to the highest or lowest comparables, the appraiser must explain and substantiate with market data why the chosen comparables are the most reliable. Often the best comparables are those that require the least amount of adjustment.

   b. Just as the most appropriate rent comparable must receive more weight, the general health of the rental market must be recognized before relying upon one or two optimistic indicators.

C. On LIHTC and/or bond financed projects, the Form HUD-92264T must be completed to determining the appropriate processing rents.

D. Rents as of the appraisal date or market study date. Rental estimates shall be made as of the appraisal or market study date and may not be trended to a future date. Since rent estimates are made based on street rents currently being obtained by the comparables, no time adjustment is needed for an estimate as of the appraisal or market study date.

E. Equipment included in the subject rent must be identified–such as ranges, refrigerators, microwave ovens, air conditioning equipment and laundry facilities. Services included in the subject rent frequently include heat, air conditioning, water, and trash removal. Comparable project equipment and services must correspond to the same items of equipment and services provided in the subject proposal and the adjustment process must reconcile any differences. This analysis also applies to the analysis of expenses.

F. Vacancy and Collection Losses.

1. The appraiser must establish a factor for vacancy and collection loss when determining the effective gross annual income for the residential units. The factor must consider both historical and current data (applicable for existing properties) of the subject property, the rental comparables and any anticipated changes in the market. The factor selected must reflect long-term occupancy rates that are expected to continue.

2. The estimate of occupancy should be based on the actual occupancy of the subject without regard to programmatic constraints imposed on the maximum underwritten occupancy when calculating debt service coverage. The estimate of occupancy should take into account the vacancy and collection loss typical for the subject's market area and, if applicable, be consistent with the subject's historical performance.

G. Commercial Income. Where commercial facilities are included in a mixed use project, a separate analysis must be made of the effect that the commercial operation will have on the project. The appraiser must calculate income, vacancy and collection loss, operating expenses, and replacement reserves attributable to commercial space separately from the residential space. Project paid resident improvements must be accounted for as a leasing expense, and if applicable, a separate commercial-space operating deficit must be calculated in addition to the required residential operating deficit. A separate analysis must be performed for each type of space using the Form HUD-92273 or a similar format to summarize appropriate adjustments to comparable data. These studies can be incorporated as a separate section in the overall residential market study submitted at the pre-application or firm stages, depending on the program requirements, and must also comply with Appendix 7A. Care must be taken in reviewing the allowable square footage and income percentage attributable to the commercial/office space since these requirements vary by program. See Chapter 3 for a more complete synopsis of space and income limitations.

Unlike the valuation of the residential portion of a mixed use project, when establishing the value of the commercial portion of the project, the appraiser must apply the same programmatic limitations on commercial occupancy; space and income as are imposed by the programs when establishing the commercial NOI for calculating debt service coverage (see Chapter 3).

1. The appraiser must: Conduct a complete analysis of at least three commercial income and expense

comparables and provide for each comparable a photograph, the resident's name, type and address of business, square feet, rent, vacancy, any concessions and major lease terms. Provide data to support the subject's commercial vacancy rate in relation to the market commercial vacancy rate and review the rollover risk and cost of resident improvements to re-lease space. Use a vacancy factor of not less than 10% for Section 223(f) and 20% for Section 221(d), and Section 220 new construction/substantial rehabilitation to obtain effective gross commercial income for underwriting purposes. Provide for each lease, the term, commencement date, expiration date, and name of the resident, square footage, and calculation of gross rents, expenses, reimbursement of expenses, cancellation clauses, and renewal clauses.

2. Limitations on the amount of commercial space and income vary by program (see Chapter 3) and must be applied in the valuation analysis.
3. The project expense estimate must include all commercial expenses payable by the project owner. The analysis of all commercial income and expenses must be reflected on Form HUD-92264 with all the supporting data attached to the form.

H. Project Rent Concessions. Rent concessions in comparable projects must be included in the analysis and an appropriate adjustment made to the subject rent based on the comparable units. The adjustments must reflect the actual impact on gross annual income resulting from the comparable rental concession.

I. Occupancy. When the occupancy rate in a comparable project is significantly less than the long-term occupancy rate estimated for the subject, a downward adjustment should be made to the comparable's rent. If other factors such as condition have had an effect on occupancy, care should be taken to avoid excessive and duplicative adjustments for interdependent factors.

J. Utilities/Services. All of the items for consideration under this heading refer to the cost of the services of water, sewer, gas and electricity that may be included in the rent. In some cases, even though both the subject and the comparable units have the same service included in the rent, an adjustment may still be warranted to bring the comparable in line with the subject, due to size, equipment, utility rate, type of utility, etc. If included in the comparable rent, but not in the subject, enter a negative adjustment reflecting the portion of the comparable's rent attributable to the inclusion of the service. If excluded from the comparable rent, but included in the subject rent, enter a positive adjustment reflecting the estimated increase in rental value attributable to including the service in the subject's rent.

K. Project Location. Consider the subject location relative to distance from shopping, recreational, social, and medical and employment centers, neighborhood desirability, transportation, special hazards and nuisances.

L. Project Amenities and Other Factors.

1. Among those "other" items that may be considered, but are not limited to, are the following:
   a. Livability–reflect good or poor unit design and configuration, including room sizes, layout adequacy of closets, lighting, elevators and laundry facilities, etc.
   b. Condition of improvements–reflect lack of maintenance, soundproofing, etc.
   c. Parking–reflect parking rates, adequacy of parking for visitors, proximity of parking to the units, inclusion/exclusion of parking space with unit rental, etc.

d. Project density–consider open space or crowding of units, if the degree of either is such that it would affect the level of attainable rental.

e. Unit location–reflect here features of location of unit within the project, such as view, proximity to swimming pool, tennis or other recreational facility, and/or other such factors.

2. Generally, only high-rise elevator comparables are to be compared with the subject elevator high-rise proposal. Mid-floor level rents of the comparables are compared with the mid-floor level of the subject project. Adjustments for heights of the comparables above and below the mid-floor level of the subject also must be made, as indicated by the market.

M. Other Income

1. Ancillary Income. The appraiser may consider other income from resident related sources including, but not limited to, laundry facilities, parking, and other recurring and reliable sources such as equipment rental, vending machines, and cable fees in the calculation of other income based on the operating history of the project, if applicable, and whether income from these sources are common in the market. The appraiser can consider the net amount of this other income based on the actual or projected (as appropriate) amount received, adjusted for vacancy and income loss. The analysis must be discussed in the Remarks Section of Form HUD-92264.

2. Commercial Income. The term "Commercial" is applied to any space or facility permitted and acceptable for "Nonresidential Use" from which income is derived or anticipated. Income from residents for the use of facilities such as community rooms and parking are not considered commercial even though fees may be collected. This income is considered as ancillary income and is treated separately (as noted above) from commercial income. However, income related to parking or other community facilities from non-residents must be treated as commercial income and is subject to the restrictions on the underwritten occupancy rate as noted in Chapter 3. The space occupied by parking and community facilities is not included in the calculation for allowable commercial space.

3. Short-Term Lease Premiums. Projects with lease terms that are less than 30 days are not eligible for HUD-insured financing under any circumstances. Income from other short-term leases may be considered to the extent that it is present in the local market. There must be a thorough discussion of the prevalence of short-term leases in both the appraisal and underwriting summary. The amount of the premium is the difference between the rent for a unit with a term that is typical for the market (generally one year) and the rent for a short term lease. This premium is resident-related and is treated as ancillary income. Units with short term leases do not require a separate Form HUD-92273, but the rental amount must be based on market information.

4. Corporate Leases. Corporations and businesses are eligible residential residents in insured projects, so long as the lease term exceeds 30 days although compliance with the policy on Short-Term Lease Premiums is required. For underwriting and valuation purposes, the percentage of total gross income obtained from corporate leases shall not exceed 10%.

5. Ineligible Income. Ineligible income should be noted and discussed in both the self-contained appraisal report and the remarks section of the Form HUD-92264. There is no prohibition on this category of income but it cannot be included in the income calculation for the purposes of

determining value or the maximum insurable mortgage. Ineligible income includes the following:

a. Interest Income. The appraiser must not include in the calculation of income any interest income, including interest on reserves.

b. Ineligible Fee Income. Non-recurring and non-regular income that is not reliable may not be included in the calculation of income. Examples include, but are not limited to pet fees, pool fees, forfeited security deposits or forfeited rent.

c. Furnished Units. Furnished units must be underwritten at the same rental rate as for unfurnished units. This applies to all units, including for corporate and short-term leases.

6. Non-Shelter Services/Elderly Developments. Refer to Section 3.4.S.

7.8 Operating Expense Estimates

A. Purpose. A determination is to be made of the portion of gross income which must be used to maintain, operate and repair the property and to defray the costs of ownership. An accurate analysis of operating expenses is essential to determining a realistic net income estimate for the project.

Form HUD-92274, Operating Expense Analysis Worksheet, is to be used for the development of project expense estimates for Section E of Form HUD-92264, Project Income Analysis and Appraisal. Form HUD-92274 will be prepared for all cases and must be included in the processing file as supporting documentation for Form HUD-92264.

B. Sources of Expense Data.

1. For new construction projects, operating expenses must be estimated on the basis of comparable projects.

2. For existing projects, operating expenses must be adjusted on the basis of comparable projects, but will primarily be based on the past 3 years of operating experience for the subject project. In addition, the Lenders should provide trailing 12 months of income and expenses for the appraiser to compare to the historical statements.

a. The most current year property financial statement must have a third party CPA or IPA review. Owner certified financial statements may be submitted for the years prior to the last full Fiscal Year. Any owner-certified financial statement or owner-certified balance sheet and operating statement must include the following acknowledgment:

"WARNING: 18 U.S.C. 1001 provides, among other things, that whoever knowingly and willingly makes or uses a document or writing containing any false, fictitious, or fraudulent statement or entry, in any matter within jurisdiction of any

department or agency of the United States, shall be fined not more than $10,000 or imprisoned for not more than five years, or both."

b. Exceptions. For refinance transactions where the project may not have been under the current ownership for the 3-year period, financial statements for the entire 3 years may not be available. This is particularly true for bankruptcies or the acquisition of defaulted properties. Also, in purchase transactions, not all the required information may be available for reasons beyond the purchaser's control. In these situations, the borrower must submit a statement through the Lender that explains why all the required records are not obtainable. The Lender must also certify that they have evaluated the borrower's statement and agree that the information is not available. After reviewing the two aforementioned requirements, the Hub Director may waive the requirement for past 3-year period financial statements. However, the borrower must submit the project financial statements that are available including an owner-certified year-to-date balance sheet and operating statement.

3. All projects must be analyzed as independent operations and must not reflect shared expenses from nearby projects under the same management, including shared insurance premiums. If the nearby project should be subject to foreclosure, the subject project would be adversely affected, thereby constituting an unacceptable underwriting risk. Furthermore, for the same reason, estimated expenses must reflect typical long-term operation and must not reflect a specific sponsor or management entity whose operation would not be typical.

C. General: Operating expenses are periodic expenses needed to maintain the property and to continue the production of effective gross income. For appraisal purposes, an operating statement that conforms to the above definition of operating expenses may differ from statements prepared for accounting purposes. Current or historic statements must be prepared on a cash basis. It is important verify the accounting basis for the operating statement, since project operating expenses for appraisal purposes must be reported on a cash basis. Typical categories of expenses are as follows:

1. Fixed Expenses. Fixed expenses are those that generally do not vary with occupancy and have to be paid regardless of whether the property is occupied or vacant, and generally do not fluctuate greatly from year to year. Real estate taxes and insurance costs are typically included as fixed expenses.
2. Variable Expenses. Variable expenses are operating expenses that vary with the level of occupancy or the intensity of property operation. Operating expenses for large properties frequently list many types of expense variables, but typical broad categories include the following:
   a. Management charges
   b. Utilities – electricity, gas, water, sewer charges
   c. Heating and air conditioning (HVAC)
   d. General payroll and security
   e. Cleaning expenses
   f. Maintenance and repairs

g. Decorating
h. Grounds maintenance
i. Exterminating
j. Trash removal
k. Miscellaneous (supplies, etc.).

3. Reserve for Replacements. This reserve category provides for the periodic replacement of the building components that wear out more rapidly than the building shell itself and must be replaced periodically during the building's economic life. These components may include but are not limited to roof covering, carpeting, plumbing fixtures, appliances and HVAC. The estimate of the reserve for replacements should be based on reserves that are typically collected for comparable properties in the subject's market area, without regard to FHA programmatic requirements and formulas used for determining the required replacement reserves when calculating debt service coverage.

4. Total Operating Expenses. Total operating expenses for residential properties are the sum of the fixed expenses and variable expenses updated to the appraisal date, plus the reserve for replacements.

5. Commercial Facilities. Where commercial facilities are included in the subject project, a separate analysis must be made of the effect that the commercial operation will have on the project expense estimate.

D. Estimate of operating expenses by units of comparison. Items of expense shown under each comparable and the expense items applicable to the subject proposal reflected in a suitable unit of comparison–such as expense per unit per annum (PUPA), expense per room per annum (PRPA), and expense per square foot of net rentable area per annum (PSFPA), or percent of effective gross income. The expense comparables and units selected must be as similar as possible to the subject project and units as they relate to the subject location, structural type, number of bedrooms, and average unit size.

For consistency purposes, expense components must be expressed in the same units of comparison so that the expenses for the subject proposal can be totaled. However, if the unit of comparison for a specific component is different from the basic unit of comparison for the other expense items, this different unit of comparison must be explained in the expense narrative. The dollar amount of the expense item can afterwards be converted to the same unit of comparison selected for the other expense components. Additional documentation must be submitted, as needed, for all component estimates that are not self-explanatory.

E. Expense Comparables. All insured properties used as expense comparables must be identified and disclosed in the appraiser's Form HUD-92274, expense analysis and in the appraisal, except as noted below.

1. General Requirements. All comparables (confidential and disclosed) must be representative of the physical and location-specific characteristics of the subject property. Appraisers must always present the best comparables available for their analysis and must refrain from

repeatedly using the same disclosed comparable merely to meet the disclosure requirement.

2. Confidential Expense Data. The appraiser may include confidential expense comparables in the expense analysis however the analysis must include at least one fully identified and disclosed expense comparable to serve as a benchmark. Appraisers may only use confidential expense comparables that are supportive and consistent with the fully disclosed comparables used in the analysis. When submitting confidential expense comparables, the appraiser must redact only the minimum amount of information necessary to protect the confidentiality of their client. The city, state, and general market area within the city must be disclosed unless this information would clearly identify the comparable and thus breach the appraiser's confidentiality requirement. The property description, unit mix, and the physical characteristics of the comparable's units must be disclosed. It is unacceptable for the appraiser to base conclusions on confidential expense comparables that are not supported by the fully disclosed comparables used in the analysis.

3. Review of Insured Expense Comparables. The HUD review appraiser will compare the FASS or OPIIS systems file for the insured expense comparables used by the appraiser to confirm the data. In order to accomplish this, the HUD review appraiser will combine the following accounts: Acct. No. 6263T, Administrative Expenses (subtract Acct. No. 6203, Conventions and Meetings, and 6370, Bad Debts), Acct. No. 6400T, Utility Expenses, Acct. No. 6500T, Operating and Maintenance Expenses, and Acct. No. 6700T, Taxes and Insurance.

F. Expense Adjustments. Project expenses must be expressed in the same units of comparison in order to ensure accurate adjustments and correct reporting of expense estimates. Consistent adjustments for significant differences between the comparables and the subject units shall be derived from the market and applied to the subject expense estimate.

The appraiser must enter the dollar amounts attributable to significant differences between the subject proposal and each of the expense comparables–such as for physical characteristics, equipment, services provided, the level of management furnished to residents and any differences in rates between tax and utility jurisdictions. The process of correlation must be used to correlate the comparable expense for each component which is applicable to the subject project.

G. Updating Procedures. Appraisers must not trend expenses to reflect a time adjustment from the effective date of the most recent expense comparable to the anticipated date of project occupancy following construction and initial endorsement. Instead, expense estimates must be effective as of the date of the appraisal and must reflect the same year of operation.

The appraiser may use a factor expressed as a percentage to adjust expense comparables up to the same date as the most current expense comparable in order to make a more creditable comparison. However, if all of the expense comparables have data from the same operating year, no adjustment for updating is necessary.

Adjusting expense data is a two stage process, as follows:

First, the oldest comparables are updated to the date of the most recent comparable, so that all comparable data is representative of the same effective time period. Second, after updating the comparables to the same effective time period, the line items are correlated and the subject's

expense estimate is updated to the date of the appraisal.

1. The most current comparable is entered in the first column on the HUD 92274. This comparable serves as the benchmark for updating the remaining comparables.
2. The effective date of the operating expense data is always the beginning date of the operating year, for example the beginning date of a financial statement dated January 1st to December 31st is January 1st of that year. If the financial statement fiscal year ends June 30, 2000, the beginning date is July 1, 1999.
3. Other than the first comparable being the most recent, the remaining comparables do not necessarily need to be in chronological order.
4. The appraiser must enter the comparable's itemized expenses as reported on audited, reviewed or certified financial statements. Per unit expenses or per square foot expenses are treated similarly:
   a. The actual expense amount must be entered in the first column, without any adjustments.
   b. Once the adjusted per unit expenses are determined for each comparable, the subject property's expenses are then correlated from the array.
   c. Once the correlated line item expenses for the subject property are determined, they are added and updated to the date of the appraisal.
   d. The correlated subject expenses are updated based upon the beginning date of the expense period of the most recent (the benchmark) comparable. HUD may request from the appraiser the names and addresses of any confidential expense comparables used in the expense analysis, pursuant to the Confidentiality sub-section of the Ethics Rule, along with Standards 3.1.e and 3.2.f of the USPAP. If the appraiser still refuses to provide this information, the HUD appraiser may request additional non-confidential comparables.

H. The expense line items included in the Section E. of HUD-92264 should be consistent with the individual line items as updated, on the HUD-92274.

7.9 Site Analysis

Key analyses for consideration of site acceptability for a proposed project are as follows:

A. Analysis of Location. The analysis of location involves a determination of the desirability and utility of the site, probable future neighborhood trends, the pattern of property and neighborhood improvements and rents in the area.

B. Specific Location. Consider the specific site in relation to neighborhood and city-wide physical, social, and economic influences, limitations of use imposed by zoning or deed restrictions, development trends, stability, decay, and rehabilitation, availability of utilities, services, and appropriateness of the intended use. Review and analyze the various influences which affect its market and income potential, including a review of the crime rate in the area, its impact on the project and how the impact, if any, can be addressed through design or staffing. (For further guidance, consult USPAP Advisory Opinion 16, "Fair Housing Laws and Appraisal Report Content").

C. Civic, Social and Commercial Centers. Consider the sufficiency of community facilities as they relate to the needs of residents of the proposed project. A location for a multifamily project must be adequately served by elementary and secondary schools, neighborhood shopping centers, transportation, churches, playgrounds, parks, libraries, hospitals, and theaters and other appropriate services.

1. Schools. Accessibility to schools will be judged by the transportation time required, rather than by walking distance alone. Thus, if school bus service will be provided and the time involved is reasonable, the location may be acceptable even if schools are not within walking distance. School capacity is the responsibility of the community and a project that is otherwise feasible will not be rejected because the local schools are considered overcrowded, unless it can be proven that marketability is adversely affected.
2. Neighborhood Shopping Centers. The convenience of shopping should be judged on the basis of time rather than distance. The importance of grocery, drug, and other neighborhood shopping facilities to be within a reasonable walking distance will be heightened based on the number of residents who do not have private transportation.
3. Religious and Recreation Centers. Ready access to religious and recreation centers is desirable. Projects designed for large families have a greater need for playgrounds and active recreation areas. Adequate on-site provisions for playgrounds and other recreation amenities must be incorporated into the proposal where adequate facilities are not in close proximity to the project site and available for use by occupants.

D. Transportation. Convenient transportation to places of employment, major shopping districts, civic and social centers is a prerequisite to site acceptability. In those communities where local public transportation is the principal means of commuting by the prospective residents, the location of a project designed for such occupancy shall be within a reasonable walking distance to mass transit.

E. Special Hazards and Nuisances. Such conditions include unusual topography, subsidence, flooding, unstable soils, unusual traffic hazards and noise, danger from fire and explosion, exposure to airport noise and low-flying airplanes, smoke, chemical fumes, noxious odors, stagnant ponds or marshes, and sewage disposal failure. Any of these, or similar conditions, if serious and infeasible to overcome, will cause a specific location to be ineligible for mortgage insurance.

F. Parking Facilities. Consideration must be given to the effect on parking facilities in the neighborhood and on all-night parking, in particular, which would be caused by the additional number of cars of the residents who would live in the proposed project. If the project site lacks adequate space for parking residents' cars, the availability of other off-street parking space must be considered. An estimate must be made of the number of parking spaces which would be required by the residents of the proposed project and their guests and a recommendation must be given as to the adequacy of the parking facilities to meet the estimated need of residents.

G. Site Suitability. The site must be adequate in size, shape, exposure, and contour for the proposed project. Building height limitation, project unit size and numbers, necessary on-site parking and play areas must be considered.

H. Sites/Projects Sold by a Public Body.

1. The Market Value of Land Fully Improved or the "As Is" Value of a Proposed Substantial Rehabilitation Project. For underwriting purposes, where sites/projects are sold by a public body to the developer for a specific re-use purpose, the value of land fully improved is the lesser of:

   a. The amount found by comparison with other sites having the improvements and amenities that the subject site will have upon completion.

   b. The dollar amount paid by the purchaser under the purchase contract with the public body, plus an estimate of any additional costs imposed by its terms or by the insurance program. Such costs are those to be borne by the purchaser under the purchase contract, including, real estate taxes and special assessments accruing from date of purchase to date of commitment, legal fees incident to the land/project purchase, re-zoning costs, installation of certain designated off-site improvements, razing structures and clearance of the site (after allowance for any income to the purchaser). This is not a complete list of items covered, but will serve as a guide to the acceptability of costs required by the purchase contract.

When the subject is a site or project sold by a public body, the appraiser must still provide an estimate of the true market value of land or the "as is" market value of an existing project, as if it were sold by a private owner. This should be noted in the remarks section of the Form HUD-92264.

2. "As-Is" Value of Land. HUD's estimated value of land or project "as is" for cost certification may include all of the items in paragraph 1.b above with the following exceptions: Installation of off-site improvements and cost of razing structures and clearing the site (less income received). This is intended to avoid duplication of costs that might be reflected in the estimated value of land "as is" and also allows for the sponsor to include them as separate items in cost certification which includes both off-site costs and demolition. The dollar amount of the land purchase contract plus a breakdown of the estimate of additional costs must be fully itemized and documented.

I. Site Value for Subsidized and/or LIHTC Projects: The site value is to be estimated using a capitalization rate and property NOI as if the units and the property were unrestricted and market rate, without considering: a) any additional value that may be attributable to subsidies available to the project or to any LIHTCs or other tax benefits the property will receive, or b) any value reduction due to any NOI or value limitations caused by regulatory agreements or affordability restrictions imposed by any subsidy program or tax regulation. This valuation methodology permits sponsors to acquire property at its market value for new construction or rehabilitation of affordable housing. The value attributable to the presence of LIHTC's diminishes over time and is not always freely transferable, and thus should not be taken into consideration.

J. Warehousing of "excess" land area is not encouraged but where un-avoidable, it may be

permitted but may not be funded with insured mortgage proceeds.

7.10 Pre-Application Stage for Sections 220, 221(d) and 231

A. Exhibits:

1. Application for Multifamily Housing Project, Form HUD-92013
2. Location map
3. Phase I ESA with a narrative environmental report. If the Phase I Assessment indicates a need for further study, a Phase II Assessment should also be submitted.
4. Evidence of site control (deed, purchase agreement, or option)
5. Market Study
6. Estimate of Market Rent by Comparison, HUD-92273
7. Photographs and location map of rental comparables used in the HUD-92273 analysis.
8. Operating Expense Analysis Worksheet, HUD-92274
9. Estimate of the warranted price of the land for new construction or the "as is" value of the land and building for substantial rehabilitation cases.

B. Lender's responsibilities:

1. Based upon the market study prepared by the market analyst and the rental income and expense estimates prepared by the appraiser, the Lender is responsible for making the following determinations before submitting the application:
   a. Determine the current occupancy levels, market absorption rates and market demand for the number and type of units proposed.
   b. Analyze site for acceptability.
   c. Determine market rents reflecting amenities, services, equipment offered and estimate project income.
   e. Estimate total operating expenses.
   f. Estimate mortgage amount based on HUD-92264-A, Criteria 5, Debt Service Ratio.
   g. Make a determination of feasibility or non-feasibility of the sponsor's proposal.
   h. Evaluate the market study and appraisal report. The Lender will either accept their conclusions for use in underwriting, or may revise them for underwriting purposes. Any such revisions must be explained and justified. The Lender may adjust the appraised value downwards but may not adjust it upwards.
2. The Phase I ESA report must be prepared in accordance with Chapter 9 and the Lender should advise the market analyst and the appraiser of any conditions which might affect the marketability or value of the property.
3. The appraiser or market analyst must prepare the market study in accordance with the

requirements of this Chapter.

4. The appraiser must determine project rents, estimated rental income, operating expenses the warranted price of land or "as is" value (of land and buildings for substantial rehabilitation cases). The Lender must assure that the forms HUD-92273, Estimate of Market Rent by Comparison, and HUD-92274, Operating Expense Analysis Worksheet, are prepared. The forms and specific instructions to complete them are found in the MAP Forms Book. For substantial rehabilitation projects, the appraiser must estimate the rents and expenses based on the assumption that all proposed substantial rehabilitation to the project has been completed.
5. The Lender must consider cost information from various sources, including the sponsor, appraiser, and cost consultant (including soft-cost and land cost information) to calculate the total replacement cost and will compare its estimate of total replacement cost with the costs estimated by the borrower.
6. Complete the HUD-92264, HUD92264-A, and supporting forms.
7. The Lender must compare the calculations on the HUD-92013 with those proposed by the borrower and either accept the borrower's proposal, recommend its modification, or reject it and advise the borrower that the project is infeasible.

C. HUD Review:

1. The Lender must submit the exhibits listed in Section 7.10.A to HUD.
2. The HUD appraiser and the EMAD economist must each provide a desk review of the market study. The HUD appraiser must make final recommendations to the team leader regarding market demand for the project.
3. The HUD appraiser must inspect the subject site and all of the comparables used in the appraiser's HUD-92273 and HUD-92274 analyses.
4. The HUD appraiser (or other designated Environmental officers) must review the Phase I ESA, and complete the HUD-4128, "Environmental Assessment and Compliance Findings for Related Laws" and the sample field notes checklist.
5. The HUD appraiser must review site characteristics and make a recommendation regarding site acceptability to the team leader.
6. The HUD appraiser must determine that the comparables submitted are acceptable.
7. From a review of Forms HUD-92264, HUD-92273 and HUD-92274, and supporting information, the HUD appraiser must make a recommendation (format in Appendix 7) to the team leader regarding:
   a. The acceptability of the proposed rents and estimated rental income.
   b. The acceptability of the total operating expenses.
   c. The acceptability of the site and the estimated warranted price of land or "as is" value.
   d. Any recommended modifications necessary to approve the application instead of a categorical rejection. Any value conclusions made by the HUD review appraiser that differ from the appraisal under review require preparation of a work file in accordance with Standard 1 of USPAP.

7.11 Firm Commitment Processing for Sections 220, 221(d) and 231 (New Construction)

A. Exhibits:

1. Application for Multifamily Housing Project, Form HUD-92013
2. Evidence of permitted zoning
3. Evidence of last arms-length transaction and price
4. Appraisal
5. Rental Housing Project Income Analysis and Appraisal Form, HUD-92264
6. Supplement to Project Analysis, HUD-92264-A
7. Updated estimates of Market Rent by Comparison, HUD-92273
8. Updated operating Expense Analysis Worksheet, HUD-92274
9. All exhibits for HUD to complete the Environmental Assessment and Complete Findings for the Related Laws (HUD-4128), including any documentation that was required as a result of findings made during Pre-Application processing.

B. Lender's Responsibilities:

1. Contract for an appraisal establishing the replacement cost for the project utilizing the cost approaches in accordance with requirements found in Section 7.6. The appraiser will update the rental and expense analyses provided in the Pre-Application.
2. The appraiser is also required to determine the "warranted price of the land" for new construction projects and the "as is" value of the property for substantial rehabilitation projects. In addition, for Section 231 substantial rehabilitation projects, the appraiser must also determine the "value fully improved" of the project site.

3. The Lender must forward or otherwise coordinate sharing information prepared by its cost analyst and any soft-cost and land cost information provided by the sponsor with the appraiser for assistance in the calculation of the total replacement cost.

   In accordance with USPAP Standard 2-3, "When a signing appraiser(s) has relied on work done by appraisers and others who do not sign the certification, the signing appraiser is responsible for the decision to rely on their work. The signing appraiser(s) is required to have a reasonable basis for believing that those individuals performing the work are competent. The signing appraiser(s) also must have no reason to doubt that the work of those individuals is credible."

4. The Lender must assure that all applicable sections of the Rental Housing Project Income Analysis and Appraisal, Form HUD-92264, found in the MAP Forms Book, are completed in accordance with specific instructions for the form, for the type of project proposed.

5. HUD-92664 items to be calculated by the appraiser include:

a. Market rents and estimated income

b. Estimated total operating expenses

c. Total estimated replacement cost of the project

d. "Warranted Price of the Land" for new construction projects and the "As Is" value of the land and building for substantial rehabilitation projects

e. Estimate of operating deficit and replacement reserve

f. Estimate REL

g. Estimate of Interest during Construction (line 53 in section g of Form HUD-92264), to be calculated as the greater of:

(1) By formula. The amount of the mortgage multiplied by 0.5, multiplied by construction interest rate and multiplied by construction years. (Construction Years is the construction time in months from line 52 in section G of the Form HUD-92264 plus 2 months, then divided by 12)

(2) Lender's estimate (optional). The Lender's estimate of interest during construction must be documented with a pro-forma draw schedule or its equivalent, subject to USPAP Standard 3. HUD's review appraisers have the option to modify appraisal conclusions internally or to return the application to the Lender for modification. See Chapter 11 Section 11.2 for review by MF Hub/PC staff.

6. The Lender must provide written explanations in the underwriter's narrative of any major changes to the pre-application invitation letter.

7. Any inconsistency between the data reported on a HUD-92264 prepared by the appraiser and the Lender's HUD-92264 must be explained in the Underwriting Summary. The appraiser should sign the Lender's HUD-92264, or a separate HUD 92264, if they disagree with the Lender's underwriter value conclusions under USPAP Standard 3.

C. HUD Review:

1. The Lender must submit the Exhibits listed in Section 7.10.A.

2. The HUD appraiser must perform a thorough technical review of the appraisal submitted for the project, making sure that it meets the requirements of Section 7.5 including all USPAP requirements.

3. The HUD appraiser must complete Form HUD-4128 and the Sample Field Notes Checklist, if not already completed at the pre-application stage.

4. The HUD appraiser must review and approve each of the following exhibits:

a. Rental Housing Project Income Analysis and Appraisal, HUD-92264

b. Estimates of Market Rent by Comparison, HUD-92273 (updated)

c. Operating Expenses Worksheet, HUD-92274 (updated)

d. Supplement to Project Analysis, HUD-92264-A

Within these forms, the HUD review appraiser must approve, reject, or approve with required modifications the estimated income, the total operating expenses, the total estimated replacement cost, the “Warranted Price of the Land” or the "As Is" value as appropriate and other major items.

5. The HUD review appraiser must issue a written report containing recommendations and forward a copy to the team leader.
6. The HUD review appraiser must review the Underwriting Summary, including justifications of discrepancies between the Lender’s and the appraiser’s conclusions.

7.12 Firm Commitment Processing for Section 223(f)

A. Exhibits:

1. Application for Multifamily Housing Project, Form HUD-92013
2. Location map
3. Evidence of permitted zoning
4. Evidence of site control (deed, purchase agreement, option)
5. Evidence of last arms-length transaction and price
6. Phase I ESA with a narrative environment report. A Phase II ESA must also be submitted, should the Phase I ESA disclose a need for further study. This requirement applies to all 223(f) programs and 202 (202/223(f)).
7. Appraisal
8. Rental Housing Project Income Analysis and Appraisal, HUD-92264
9. Supplement to Project Analysis, HUD-92264-A
10. Estimates of Market Rent by Comparison, HUD-92273
11. Operating Expenses Analysis Worksheet, HUD-92274
12. Balance sheets and operating statements
13. Rent roll of the subject property
14. PCNA

B. Lender’s responsibilities:

1. The Underwriting Narrative must demonstrate that the MAP Underwriter performed adequate due diligence in reviewing the appraisal including a thorough discussion by the Underwriter of the appraiser’s market analysis with a comparison made to the conclusions from the market study, in cases where a separate market study is required. There must also be a full discussion by the Underwriter of the approaches to value and the appraiser’s reconciliation and value conclusion.

The Lender must state any reasons for disagreement with the appraisal report. The underwriting summary should contain a thorough discussion of any differences between the value conclusions made by the appraiser and what was actually used in underwriting the loan. The appraiser's value conclusions may be adjusted downwards by the Underwriter but may not be adjusted upwards.

2. The appraiser must complete an appraisal of the property establishing market value utilizing the cost, income, and comparable sale approaches. The Cost Approach may be eliminated at the discretion of the appraiser for subjects that are ten or more years old, although an estimate of the land value must still be provided.

3. The appraiser must participate in the inspection of the property with the Needs Assessor as described in Appendix 5H. The appraiser must consider the eligibility of the project, confirm the project occupancy level, and verify the owner's rent roll during the inspection. When the appraiser has established that the owner's rent roll is correct, the actual occupancy, based on the owner's rent roll, must be entered in the Remarks Section of Form HUD-92264. The appraiser must also determine whether the apartments are furnished or unfurnished.

4. The appraiser must analyze the property for acceptability.

5. The Lender must have the Phase I ESA and narrative report prepared.

6. The Lender must assure that forms HUD-92273, Estimate of Market Rents and HUD-92274, Operating Expense Analysis Worksheet, are completed as required by the instructions found in the MAP Forms Book. This is based on the determination made by the appraiser of the project's income and operating expenses including a review of the operating history of the property (rent roll and financial statements).

7. The Lender must assure that all applicable sections of the Rental Housing Project Income Analysis and Appraisal, Form HUD-92264, found in the MAP Forms Book, are completed in accordance with specific instructions for the forms, for the type of project proposed.

8. HUD-92264 items to be calculated by the appraiser include:
    a. Market rents and estimated income
    b. Estimated total operating expenses
    c. Total estimated replacement cost
    d. "Warranted Price of the Land"
    e. Market value of the project
    f. Estimate of operating deficit and replacement reserve
    g. Estimated and actual occupancy rate
    h. REL

9. The data provided in the Lender's HUD-92013 and HUD-92264 must be consistent and any inconsistency between the data reported on a HUD-92264 prepared by the appraiser and the Lender's HUD-92264 must be explained in the Underwriting Summary.

10. The Lender must assure that the Remarks Section of HUD-92264 contains the following information:

    a. The appraiser's statement of actual occupancy, based on the owner's rent roll.

    b. The required amount of initial deposit into the Reserve for Replacement.

    c. The estimated cost of required repairs as provided in the inspection report.

    d. The estimated amounts for legal, organizational (if applicable), title and recording expenses based on the maximum insurable loan.

C. HUD review:

1. The Lender must submit the Exhibits listed in Section 7.12.A.
2. The HUD review appraiser must perform a thorough technical review of the appraisal submitted for the project.
3. The HUD appraiser must inspect the subject site and as many of the comparables as feasible, that were supplied by the appraiser. At this visit, the HUD appraiser will also review the borrower's proposed list of critical and non-critical repairs and provide an opinion of the acceptability of the list based upon the HUD appraiser's potentially limited knowledge of construction. The HUD appraiser may consult with a HUD construction analyst when formulating the opinion.
4. The HUD appraiser must complete Part A of HUD-4128.

   The HUD appraiser must review the recommendations of the HUD architectural analyst and the HUD-92264, and must review property characteristics and, based on these reviews and the environmental analysis, must make a recommendation of site acceptability.
5. The HUD appraiser must review and approve each of the following Exhibits:

   a. Rental Housing Project Income Analysis and Appraisal, HUD-92264

   b. Estimate of Market Rent by Comparison, HUD-92273

   e. Operating Expenses Worksheet, HUD-92274

   The HUD review appraiser must approve, reject, or approve with required modifications of major items including the estimated income, the total operating expenses, the total estimated replacement cost, the estimated REL, the maximum insurable mortgage and the market value of the project.
6. The HUD appraiser must review the Underwriting Summary for justifications of discrepancies between the Lender's and the appraiser's conclusions.
7. The HUD appraiser must review the Underwriting Summary to determine if the Lender's underwriter carried out a "due diligence" review of the appraisal.

8. The HUD appraiser must issue a written report containing recommendations and forward a copy to the team leader.

7.13 Substantial Rehabilitation Processing for Sections 220 and 221(d)(3), 221(d)(4) and 231

A. In general, a substantial rehabilitation project is processed in accordance with the instructions found in Sections 7.10 and 7.11, except as noted below.

B. Form HUD-92264 must be completed in accordance with basic valuation instructions for Sections 221(d) and 220 processing, with the following modifications:

1. "As Is" Value. Development of the "As Is" value must be in accordance with the pertinent requirements of Standards 1 and 2 and the applicable approaches to value. A supplemental HUD 92264 is not required.
2. The HUD-92273 and HUD-92274 analysis used to support the income and expenses on the HUD-92264 must reflect the "as completed" property conditions that will exist after substantial rehabilitation has taken place.
3. A value for the land without improvements must be estimated and entered using the analysis grid in Section H of the HUD 92264.
4. The "as is" value and the value of the land without improvements must be entered in Section "O" (Remarks) of the HUD 92264.

C. Applicable Approaches - "As Is" Value in Substantial Rehabilitation: The estimate of "As Is" value of the land and building before rehabilitation should be estimated by the direct market comparison approach and the income approach to value. The "As Is" value by the residual approach is not mandatory, but can be used in cases where there is a lack of market sales. The Market Value by the market comparison approach will be based upon market prices for comparable properties in similar condition to the project being appraised. The income approach may not be feasible for the valuation of properties in extremely poor condition or are mostly or entirely vacant, boarded up or abandoned for an extended period to time.

D. Valuation Processing: (Sections 220, 221(d)(3), 221(d)(4))

1. Determine the market value of the property "As Is". Complete the Location and Description of the Property, Information concerning Land or Property, Estimate of Income, Equipment and Services Provided in Rent, Estimate of Annual Expenses, Income Computations, and Income Approach to Value, and Sales Comparison Approach to Value within the report. If the project involves rehabilitation and new construction with additional land to be added, also complete a land appraisal for that portion of the land to be added for the new construction portion of the development proposal.
2. Use the Replacement Cost by Formula, Rehab Projects, with or without BSPRA, found in the MAP Forms Book to find the total project cost (summation estimate) using the "As Is" market value of the property, and the rehabilitation cost estimate furnished by the cost analyst, plus

carrying charges and financing.

3. Complete HUD-92264. In Section G, the "As Is" market value of the property before rehabilitation will be shown on the line titled "As Is" value of property.
4. "As Is" value of property acquired as a leasehold estate. Instructions for limiting the "As Is" value of property before rehabilitation, when that property is acquired as a leasehold estate, are found in Ground Leases, Section 7.16.
5. To find the project mortgage amount for Section 220 and Section 221, use the lower of Criteria 1, 3, 4, or 5 on HUD-92264-A. Estimate the "As Is" value of the property before rehabilitation, add the total for all improvements plus soft costs to the As-Is Value to obtain the sum of the above costs. Then multiply the sum of the project costs listed above by 90 percent based upon Criterion 3 to obtain the maximum project mortgage amount. Under the Section 221(d) (3) program for nonprofit borrowers, multiply 90 percent against the sum of the project's cost.

E. Valuation Processing for Section 231 Substantial Rehabilitation Cases. Section 231 substantial rehabilitation cases requires two value estimates, a value subject to the completion of rehabilitation using all applicable approaches, which shall be used in Criterion 3 of the Form HUD-92264-A, and an "As Is" value entered in Section G, line73b of the Form HUD-92264 to determine the Total Replacement Cost of the Project, in a manner similar to the procedure used in Sections 220 and 221(d) (3 & 4). Depreciation is not included. The "As Is" value is also used in completing Criterion 6 of the Form HUD-92264-A.

If the Total Estimate Replacement Cost of the Project (Line 74 of Section G of the 92264) exceeds the value after rehabilitation, the residual. "As Is" value by formula must be completed (see MAP Forms Book). This amount must be entered on line 73b of Section G, and Section G, line 74 will be considered to be the value of the project after rehabilitation and this amount must be entered in Criterion 3 of the Form HUD-92264-A.

F. Contingency Reserves. To address unanticipated costs inherent in the rehabilitation of older structures, there will normally be included in the mortgage amount a reserve for contingencies based on the percentage of estimated rehabilitation cost without fees. This percent may range between 10 percent and 15 percent, depending upon the scope and type of rehabilitation and the experience and financial ability of the sponsor, the borrower and contractor and on whether the contractor's bid already contains a reserve for contingencies. This percentage, determined by the cost analyst, must be included as a separate line item in the estimate of replacement cost on HUD-92264.

G. Interest during Construction. Interest during construction (line 53 in section G of Form HUD 92264) must be calculated as the greater of:

1. By Formula. The amount of the mortgage multiplied by 50 percent, multiplied by construction interest rate and multiplied by construction years. (Construction Years is the construction time in months from line 52 in section G of Form HUD-92264 plus 2 months, then divided by 12).
2. Lender's Estimate (optional). The Lender's estimate of interest during construction must be documented with a pro-forma draw schedule or equivalent.

H. Inspection Fee. The inspection fee is calculated as half of one percent (0.5%) of the loan amount

when the project involves new construction. For substantial rehabilitation projects, the inspection fee is calculated as the sum of Total for All Improvements (plus BSPRA, if applicable), rounded to the next higher $100, times .5 percent.

I. Offsite costs. If there are any offsite costs associated with the rehabilitation, enter them as a line item in the Estimated Replacement Cost. This separate entry is necessary in rehabilitation processing, since the "As Is" value does not include offsite cost requirements.

J. Rehabilitation cost not attributable to residential use. This entry must be completed for all rehabilitation projects and is prepared on Rehabilitation Cost Not Attributable to Residential Use, found in the MAP Form Book, and transferred to line 4b under Criterion 4, Amount Based on Limitations per Family Unit, HUD-92264A.

K. Developer's Fee, when applicable. HUD may include in the estimated replacement cost of a project, a nonprofit developer's fee in addition to the legal, organizational and audit fees normally included in the estimated replacement cost of a project. These instructions do not apply to the refinancing of Section 202/811 projects.

1. The fee will be based on a sliding scale at eight percent of the mortgage, but not less than $40,000 or more than $400,000.
2. Exceptions:
   a. For mortgages in excess of $5,000,000 increase the maximum fee to provide an additional 2 percent based on that portion of the mortgage that is in excess of $5,000,000.
   b. At the option of the nonprofit sponsor/borrower, the fee included in the replacement cost may be reduced.
3. Part or the entire fee may be used to pay for transactional costs related to developing the subject project including but not limited to:
   a. Reduction of the estimated closing costs of the project
   b. Staff salaries
   c. Nonprofit working capital deposit
   d. Relocation expenses
   e. Operating deficit escrow
   f. Financing fees above the 3.5 percent included in the estimated replacement cost of the project;
   g. Environmental studies
   h. Housing Consultant services provided by either in-house staff or contractor
4. Funds not used to meet the estimated cash requirements of the project will be released to the nonprofit based on a percentage of completion method.

L. Items no longer included in the Estimated Replacement Cost of a Project. HUD will no longer include in the estimated replacement cost of a project, an Allowance to Make Project Operational (AMPO) and an amount for Housing Consultant services except as part of the developers fee

noted above.

7.14 Calculating Operating Deficits

A. Estimate a project's operating deficit, if any, in its early years if required by the applicable insurance program. A project which cannot rent-up to sustaining occupancy in the first years must be carefully examined and may not be financially feasible to fund. However, if it takes time to move residents into a large project, then it is likely that the average overall occupancy percentage for the first year will be less than the break-even percentage. When it is anticipated that the project's net income will be inadequate to support the insured loan during the initial rent-up period, the appraiser must estimate the anticipated project operating deficit, utilizing the following steps:

1. Estimate the total project operating expenses, add the debt service requirement (including principal, interest and mortgage insurance premium (MIP)) and divide the total by the potential gross income for the project. The resultant ratio is the break-even occupancy level. Multiply that percentage times the total project units to obtain the number of units required for break-even occupancy (rounding up any fraction of a unit).

2. Estimate the total number of units expected to be occupied at the time of Final Endorsement. The difference between the total units required for break-even occupancy and those occupied units at the time of Final Endorsement represent the total number of units that must be rented in order to reach a break-even occupancy level.

3. Estimate the likely rate of absorption of the available units, taking into account the current and proposed supply of housing units in the subject's market balanced against demographic and demand considerations. The absorption or lease-up rate must be supported by comparison to similar project's historic rates of absorption during their lease-up period whenever such a comparison can be made. The number of units to be absorbed, divided by the monthly absorption rate, will yield the total number of months of the entire operating deficit period.

   a. Absorption Period. The Absorption Period is the period of time necessary for a newly constructed or renovated property to achieve stabilized occupancy. The absorption period begins when the first certificate of occupancy is issued and ends when the last unit to reach stabilized occupancy has a signed lease and is actually occupied by a resident. This assumes a typical pre-marketing period; prior to the issuance of the certificate of occupancy, of about three to six months and the month that leasing is assumed to begin should accompany all absorption estimates. It is important to consider that the absorption of restricted/low-income units may be different, depending on the differential in rent between low-income rents and market rents, and the number of income-qualified potential residents in the HMA.

   b. Maximum Allowable Absorption Period. Previously, HUD had allowed absorption periods of up to 24 months. Due to volatility and weakness in the real estate markets, the absorption period used in estimating market demand for the proposed number of units now must be restricted to 18 months. Larger projects may phase additional units under a

separate application for mortgage insurance (e.g. under Section 241(a)). An exception to the 18-month absorption period limitation may be considered by waiver granted by the Hub Director for large high-rise buildings. Such projects will be evaluated based on their own merit and will require a larger initial operating reserve to insure against the risk inherent in a longer absorption period.

c. Absorption Rate. The Absorption Rate is the average number of units rented each month during the absorption period.

4. Because the deficit period can begin at certificate of occupancy, continue through the cost certification phase, and run into the amortization phase, there are three distinct expense intervals to consider when calculating the total deficit period, although not every project will require using all three intervals.

Interval 1 covers the period of time between certificate of occupancy and the end of the construction period/cost certification period. (Note that the construction period is defined as construction time plus two months for cost certification purposes). This is an optional interval, because some projects may have the same certificate of occupancy and construction completion dates and thus would not need an Interval 1. When calculating expenses for this Interval, no debt service is to be included as an expense since the mortgage interest for this interval is included in the mortgage in Section G Line 53 "Construction Interest". Replacement Reserves and ground rent are not to be included in Interval 1 since Section 7.16.G, requires ground rent during the construction period to be included in the mortgage. This interval must only include the appraiser's estimate of all of the applicable operating and leasing expenses for each month (period).

Interval 2 begins at the end of the construction period/cost certification process (construction time plus two months) and ends at the beginning of loan principal amortization. This period can be no greater than 2 months and is also an optional interval. (Chapter 8 Section 8.5.A requires amortization to begin "no later than 4 months after construction completion for insurance of advances and first day of second month after final endorsement for insurance of completion cases"). If amortization begins at the end of the construction period, this interval will not be necessary. Debt service must include payment of interest and MIP, but not amortization, as the beginning of amortization signals the beginning of Interval 3. (Section G Line 53 of the HUD-92264 includes mortgage interest for the construction period plus two months. If amortization is deferred until 4 months after construction completion, there will be two months of unaccounted-for interest and MIP that must be included in the IOD). Ground rent must be included if the property is a leasehold since only ground rent during construction can be included in the mortgage, and this interval begins after construction completion. Replacement reserves are not included in interval 2. This interval must include the appraiser's estimate of applicable operating expenses for each month (period).

Interval 3 begins at the beginning of amortization. Amortized debt service is mandatory in this interval, and must include payment to principal, interest and MIP. Ground rent, if applicable and replacement reserves are also mandatory in interval 3. This interval must include the appraiser's estimate of applicable operating expenses for each month (period). Interval 3 ends when NOI becomes positive and is sufficient for breakeven coverage of the

mortgage debt.

5. Operating deficits can occur before and after the start of amortization. The operating deficit calculation for the first interval must begin when the Certificate of Occupancy is secured.
6. If the dollar amount of debt service for a period is greater than the net income for that period, the difference represents the estimate of the operating deficit. One period of positive income does not cancel a prior period of income deficiency.
7. The operating deficit represents the total of all cumulative losses projected to occur before the project reaches breaks even and produces a positive cash flow. These losses may not be offset by intermittent periods of positive cash flow.

B. Where commercial facilities are included in the project, a separate analysis must be made of the effect that the commercial operation will have on the project expense estimate. A separate operating deficit estimate of income loss for commercial rent-up must be made. The appraiser must insure that expenses included in the residential deficit estimate are not duplicated in the commercial space deficit estimate so as to unfairly penalize the property. The commercial space deficit is added to the residential operating income deficit to determine the total project operating deficit escrow funding that will be necessary. Any positive income attributable to the commercial space during the deficit period will not offset the residential operating deficit requirements.

7.15 Ground Leases

A. HUD prefers to only insure mortgages for land that is owned in fee simple. For those transactions, in which fee simple ownership is not practical, the underwriting and valuation guidance in this section applies.

B. When used in this section, the words below are defined as follows:

1. Fee Simple Estate. This represents the entire ownership, from beneath the soil to the air above, enduring by inheritance and indefinitely into the future.
2. Lease. A lease is a written contract between an owner (the lessor) and a resident (the lessee) with the conditions under which the lessor will transfer the use of real property to the lessee in return for lease payments or rent.
3. Ground Lease. A long term agreement by which an owner of land (lessor) leases an unimproved site to a resident (lessee) for a term of years that is long enough to enable the lessee to construct a building on the leased site and obtain a permanent mortgage.
4. Ground Rent. Payments on a ground lease are called ground rent and must bear a reasonable relationship to the value of the site "As Is" (before construction of on-site or off-site improvements) unless the ground lease is from a governmental agency which has made the ground lease available for limited ground rent to support the development of affordable housing.
5. Leasehold Estate. The interest of the lessee under a ground lease for a term of years is called a leasehold estate. When the term of the lease expires, all rights to possession and use revert

back to the lessor/fee simple owner and the leasehold estate terminates.

6. The Leased Fee. The interest of the lessor/ fee simple owner during the period when the property is under lease.
7. In computing payments due under the lease, the terms "gross collections," "operating expenses and taxes," "net income before debt service payments" and "net cash flow" shall be defined as follows:
   a. Gross collections (or effective gross income) shall mean the annual amount collected from all sources, less refunds.
   b. Operating expenses (residential and commercial) and taxes shall be composed of items in accord with generally accepted accounting principles. However, for lease payment computations, taxes shall not include income taxes, and operating expenses shall not include interest charges, or charges or allowances for depreciation of real or personal property, or amortization of financing expense, or payments to any officer or director of the corporation, unless such payments are for services at the project which are necessary to the operation of the project. Operating expenses must include the annual amounts deposited to the Reserve for Replacement.
   c. Net income before debt service payments shall mean the annual amount which remains after operating expenses and taxes are subtracted from effective gross income.
   d. Debt service payments shall be the annual amounts paid to mortgage principal, interest, and MIP.
   e. Net cash flow shall be the annual amount remaining after debt service payments are subtracted from net income.

C. Term of Lease. Leaseholds must conform to the Lease Addendum Form HUD-92070M. The term of the Lease Addendum may vary to conform with applicable state and local law, except that the HUD closing attorney must approve:

1. The legal need for any proposed lease term changes, and
2. That any term changes are consistent with the following requirements of the Section of the Act under which the project is underwritten:
   a. Section 207/223(f) and Section 231 sub-rehabilitation. The lease term must satisfy one of the following requirements:
      (1) Term must be 99 years and be renewable, or
      (2) Term must be at least 50 years from the date the mortgage is executed. (When a lease is on trust/other land on a reservation, the HUD closing attorney must ensure that the lease provisions are coordinated with Bureau of Indian Affairs requirements).
   b. Section 220, 221(d), and 231 (new construction only). The lease term must satisfy one of the following requirements:
      (1) Term must be 99 years and be renewable, or

(2) Term must have at least 10 years remaining after the maturity date of the insured mortgage.

D. Marketability. The marketability of a rental project is based primarily on an investor's estimate of the present value of future cash flows. If a ground lease increases the project cash flow and the return on equity, investors will consider the property's marketability to be enhanced. However, the leasehold estate cannot be considered marketable unless the lease meets the requirements described of this section.

E. Regulation for Leaseholds. HUD regulations state "Reduced mortgage amount - leaseholds. In the event the mortgage is secured by a leasehold estate rather than a fee simple estate, the value or replacement cost of the property described in the mortgage shall be the value or replacement cost of the leasehold estate (as determined by HUD) which shall in all cases be less than the value or replacement cost of the property in fee simple."

F. Legal Review. The ground lease must receive both a legal review and a Lender underwriting review, neither of which may be substituted for the other. Legal review, performed by the HUD legal counsel, shall establish that the proposed lease is in conformity with the applicable statute, regulations, Form HUD-92070M (the Lease Addendum model form), and applicable provisions of local law. Any substantive deviations from Form HUD-92070M must be approved by Headquarters' Office of Multifamily Housing Development.

G. Underwriting Review of Lease at Firm Commitment. In testing the lease payments for acceptability, the appraiser must take the following actions:

1. The appraiser must perform a Firm Commitment review to develop the following estimates:
   a. Market value of land fully improved (in fee simple)
   b. Warranted price of site fully improved (in fee simple)
   c. Value of site "As Is" (in fee simple)
   d. Gross income
   e. Effective gross income
   f. Total operating expenses and taxes
   g. Net income
   h. Replacement cost by formula
   i. Value of project (in fee simple) if applicable
   j. Mortgage amount, by completing a valuation trial copy of Form HUD-92264A. (The value of the leased fee equals the value of site "As Is" in fee simple, before construction of on-site or off-site improvements.) The HUD-92264A may be completed by the Lender.
   k. Annual debt service payments to principal, interest and MIP.
   l. Annual cash flow (after debt service payments but before ground lease payments)
2. The appraiser must analyze the lease provisions that determine the amount of annual ground rent payments. Although certain kinds of ground rent payments will be permitted that increase over time, this must be accomplished without weakening the tests which are designed to assure that the position of the borrower and of the insured mortgage secured by the leasehold would be no worse than if the property were held in fee.

a. Some variable lease payments may not be acceptable because they raise the risk that future payments may be too burdensome and may cause a potential default in the mortgage payments. Examples of unacceptable methods of determining variable ground rents are:

(1) A graduated schedule of future increases on a lump sum year-by-year basis.

(2) Cost of Living Allowance (COLA) increases.

(3) Increases based on the results of future appraisals.

b. To determine if the initial amounts are within underwriting limitations, ground rents may be computed using any of the following three methods:

(1) A fixed percentage of gross collections (or effective gross income). The percentage must remain the same throughout the term of the lease.

(2) A fixed percentage of net cash flow to equity (after debt service payments but before lease payments). The percentage must remain the same throughout the term of the lease.

(3) A stated dollar amount per year which must remain fixed for at least ten years more than the term of the insured mortgage. (If monthly or quarterly payments are required, these will be converted to annual amounts by the appraiser). When the lease contains more than one method of computing lease payments, it must also indicate whether the amount to be paid is to be the greatest or the least, or the sum of these amounts. The stated annual dollar amount may be described as a minimum payment.

3. The appraiser must estimate the lease payments, using the lump sum annual amounts and percentages contained in the lease provisions, as applied to the estimated annual effective gross income or annual cash flow indicated by the appraisal and on Form HUD-92264. (The estimates are not based on the income which would be available during any period of deficit operation, but must reflect the effective gross income shown on Form HUD-92264 and the corresponding cash flow to equity which result when sustaining occupancy has been reached.).

4. Example: Assume the facts are as shown in the following example:

LAND VALUE

Warranted Price of Land Fully Improved (In Fee Simple) ..... $ 125,000
"As Is" Value of Land (In Fee Simple) 115,000
Value of Leased Fee 115,000

Income and Cash Flow

Estimated Effective Annual Gross Income, All Sources..... $ 242,455
Estimated Total Annual Expense (incl. Replace. Res.)..... 120,500
Estimated Net Income (before mortgage payments)..... 121,955
Annual Mortgage Payments (principal, interest, MIP) 99,661
Estimated Annual Cash Flow to Equity (before ground rent)..... 22,294

Estimated Replacement Cost and Mortgage Amount

Estimated Replacement Cost (or Value) of Project
(In Fee Simple)..... $1,250,000
Estimated Value of the Leased Fee 115,000

Estimated Replacement Cost (or Value) Of Project (leasehold Estate) ……..1,135,000

Maximum Mortgage Amount from Form HUD-92264-A

(Leasehold Estate) $1,021,500 ($1,135,000.00 x .90)

Annual Ground Rent Required

Assume that provisions of the lease require annual lease payments to equal the greatest of the three following calculations:

a. Three percent (3%) of annual gross collections ($242,455) =$7,274;

b. Twenty percent (20%) of annual net cash flow to equity ($22.294) = $4,459

c. Seven Thousand Dollars ($7,000.00) per year minimum.

The appraiser notes that the amount of initial ground rent required by the lease is the greatest of these three amounts: 3% of annual gross collections, or $7,274. This amount is next tested to determine whether it is within permissible limits:

a. 3% of annual gross collections ($242,455) = $7,274

b. 20% of annual net cash flow ($22,294) = $4,459

c. $7,000 per year, minimum = $7,000

The appraiser must note that the amount of initial ground rent required by the lease is the greatest of these three amounts: 3% of annual gross collections, or $7,274. This amount is then tested to determine whether it is within permissible limits.

5. Test for Acceptability of Variable Lease Payments. In the above example, the appraiser has determined that the amount of the initial annual ground rent required by the lease is acceptable.

Except for level lease payments, the annual ground rents must not exceed the value of the site "As Is" in fee simple ($115,000) multiplied by 90% of the interest rate of the insured mortgage (.90 x .09 = .081).

The following is an example of the Test for Acceptability of Variable Lease Payments:

$7,274 based on the estimate of annual gross collections (effective gross income) used in the appraisal. Thus $115,000 x .081 = $9,315. The ground rent ($7,274) is less than ($9,315) the value of the site "As Is" multiplied by 90% of the interest rate of the insured mortgage; therefore, the annual rent is acceptable.

6. Form HUD-92070M, 207 Lease Addendum. The appraiser must review other provisions of the lease (other than those concerned with annual lease payments) to determine that they will not restrict the successful operation of the project, keeping in mind that the provisions of Form HUD-92070M, the 207 Lease Addendum, must be included in, or legally appended to, the lease. The proposed lease must not contain any provisions in conflict with the lease addendum. If the above conditions are met and the annual lease payments required under the lease meet the test for acceptability, the appraiser may recommend that the lease be accepted.

7. Test for Acceptability of Level Lease Payments. The lease may only require annual ground rent payments that are a stated dollar amount per year which must remain fixed for at least 10 years more than the term of the insured mortgage. A lease may require payments that are a stated dollar amount, but may not require payments of a fixed percentage of gross collections or a fixed percentage of net cash flow (after mortgage payments but before ground lease

payments). In such cases, the amount of stated annual ground rent will be acceptable if it does not exceed the value of the site "As Is" multiplied by 100% of the interest rate of the insured mortgage.

8. Processing Single, Up-Front Payment (SUP) Leases. In ground lease cases where there is an up-front, single payment of ground rent, the 'As Is" value of the land in fee simple is to be subtracted from the property value in Criterion 3 (Line B-1 identified as "value of the leased fee") and is not to be included in the mortgage. SUP leases are treated as any other leased fee because they do not include all of the rights of fee simple ownership.

H. Ground Rent during Construction. For proposed construction under all sections of the Act, lease payments during construction must be included in the estimated replacement cost of the project and in the certified cost, subject to the following conditions:

1. The period for which ground rent is estimated must be the same as that for which interest and other related charges are calculated, or, the estimated construction time plus two months.
2. Ground rent during construction must be entered in Line G 69 of Form HUD-92264 (currently labeled "Construction Fee."). A remark must be entered in Section H, indicating that the amount in Line G 69 represents Ground Rent during Construction.
3. Ground rent must not be included in the base on which Section 220, 221(d) BSPRA is calculated.
4. The annual amount of ground rent during construction may not exceed the test for acceptability of lease payments.

I. Replacement Cost by Formula

A formula will provide the total project replacement cost and mortgage amount, based on the cost for proposed construction, where a leasehold estate is involved. This formula provides for Sections of the Act which use or which do not use BSPRA. A separate formula is necessary for leasehold properties because the mortgage amount is less than it would be if no ground lease were involved.

J. Value of the Leased Fee

1. The procedures for estimating the value of the leased fee consist of the following general rule and two exceptions:

a. General Rule. Except as provided below, the value of the leased fee must be estimated to equal the market value of the site "As Is" in fee simple regardless of whether the ground rent is an escalating amount based on a percentage of gross collections or cash flow, or whether it is a level stated dollar amount each year.

(1) The value of the leased fee, so estimated, must be entered in the appropriate space in line K-6, Form HUD-92264.

(2) The annual ground rent, based on the lease provisions and estimates of income and expense used in the appraisal, must be entered in the appropriate space in line K-6,

Form HUD-92264.

(3) Dividing the ground rent by the value of the leased fee will result in the earning rate indicated by this ground rent. This rate must be entered in line K-6.

b. Exception for Leases Containing an Option to Buy. In cases that meet the following conditions, the value of the leased fee may be estimated by capitalizing the ground rent.

(1) The lease must give the lessee an option to buy the site in fee simple for a stated purchase price at some time during the term of the lease. This stated purchase price must be provided in the ground lease and may not exceed the value of the fee estimated by the capitalization method of value at the time of property appraisal.

(2) The annual ground rent required by the lease must be level payments of a stated dollar amount and must remain unchanged from the date of mortgage endorsement to at least ten years after the mortgage term.

(3) A market capitalization rate must be used which may not exceed the interest rate of the insured mortgage. The ground rent divided by the capitalization rate results in the estimated value of the leased fee to be entered in line K-6, Form HUD-92264.

K. Option Price for Assistant Secretary for Housing–Federal Housing Commissioner. The ground lease must contain an option for the Assistant Secretary - Federal Housing Commissioner to buy out the lease. The option price contained in the lease addendum must reflect the value of the leased fee in Form HUD-92264.

L. Ground Leased from Public Bodies. On sites leased by a governmental body to a developer for use for a specific purpose, the procedures outlined in this chapter remain unchanged, except that the "As Is" market value of the site in fee simple (before construction of on-site and off-site improvements) may not exceed the value of the leased fee.

M. Rehabilitation of an Existing Leasehold Project. When a leasehold estate contains existing buildings and is to receive an insured mortgage for substantial rehabilitation, valuation processing will vary from fee simple rehabilitation processing as follows:

1. "As Is" Value of Entire Property, Land, and Buildings

a. Tentative "As Is" value of both land and building(s) must be established by capitalization of income and by comparable sales.

b. Value of the land without building improvements must be made by market comparison based on sales of similar sites.

c. Acquisition Cost of Buildings. The maximum ground rent must be limited by the value of the land without the buildings multiplied by 100 percent of the mortgage interest rate for level ground rent payments, or multiplied by 90 percent of the mortgage interest rate for acceptable escalating payments. Since the value of the land without improvements does not include buildings, the cost of the acquisition of the buildings will be whatever added cash amount the buyer pays the seller of the subject property for the buildings, at or before

initial closing. A certificate of the separately agreed amount for purchase of the buildings must be submitted with the application exhibits. In a refinancing loan which does not involve a buyer and seller, the cost of the buildings may not exceed the remaining mortgage balance.

d. Final "As Is" value of entire property is the lesser of Section 7.15.M.1.a or the sum of Sections 7.15.M.1.b and 7.15.M.1.c.

2. Value of the Leased Fee. This value will be the amount shown in Section 7.15.M.1.b, Value of Land without Building Improvements.
3. Term of Ground Lease. The term of the ground leasehold must comply with Section 7.15.C above.
4. Value of the Leased Fee. The value of the leased fee must be estimated to equal the value of the site in fee without the on-site improvements and is entered on Line K-6 of Form HUD-92264.
5. Underwriting Review of Lease. The appraiser must follow Section 7.15.H to determine whether the annual ground rental is acceptable.
6. Lease Addendum. Form HUD-92070M must be included in, or appended to and made a part of the lease. The appraiser must review all lease provisions (in addition to those concerned with annual lease payments) to determine that they will not restrict the successful operation of the project. If the above conditions are met and the annual lease payments meet the test for acceptability, the appraiser may recommend that the lease be accepted.
7. Ground Rent during Construction. For rehabilitation under all Sections of the Act, ground rent during rehabilitation must be included in the replacement cost and meet the requirements of Section 7.15.H.
8. Replacement Cost by Formula. A formula that will provide the total project replacement cost and mortgage amount, based on cost for substantial rehabilitation wherein a leasehold estate is involved, is shown in the MAP Forms Book. This formula provides both for sections of the act which recognize and which do not recognize BSPRA.

7.16 Tax Abatement Procedures

A. General Comments and Exceptions. Tax Abatement is a reduction of property taxes for a specified term by the taxing authority. Properties with abatement are eligible for additional mortgage funds under certain circumstances. <u>The abatement must run with the real estate and not with the type of sponsorship if it is to secure additional mortgage proceeds, otherwise underwriting must include an amount for property taxes in project operating expenses even if the present owner or its transferee may not pay them.</u> The risk that a transferee of the property or an assignee of the mortgage in the future might cause the tax abatement to be lost is an unacceptable risk to the insurance fund. Exceptions to these requirements include the following:

1. If the financing includes LIHTC equity and if the tax abatement runs with the sponsorship (borrower) entity, then the Hub Director may waive the MAP Guide so that the underwriting does not have to include a provision for property taxes, during the period of the tax abatement.

This exception is justified for low loan-to-value mortgages on LIHTC projects.

2. Properties leased from a governmental body to either a non-profit or for-profit developer, where the property is exempt from taxes and the abatement flows to the leasehold improvements. There is usually a requirement for a percentage of units to be set aside as affordable housing which is imposed by a land use restriction or regulatory agreement. Hub Directors may grant a waiver, after appropriate review, to promote affordable housing.

B. Long Term Tax Abatement. If the amount of the tax abatement is fixed and runs the entire term of the mortgage, the real estate tax expense reported on the HUD-92264 must be the actual amount of taxes the property will pay, if any. The full amount of the real estate taxes without the abatement must be noted in the remarks section of the HUD-92264. The property will benefit from an increased mortgage amount due to the lower pro-forma operating expenses and an increased NOI estimate. When the abatement runs for the full term of the mortgage, the NOI used for Form HUD-92264-A Criteria 5 may also be processed at the reduced tax amount. Also, if value attributable to long term tax abatement is recognized in the subject's market area, the same NOI may be capitalized and the resulting value may be used in Criterion 3.

C. Short Term or Variable Tax Abatement. If the abatement is short term or variable, it may still be used to secure additional mortgage proceeds. The additional mortgage will be the amount that will amortize over the term of the tax abatement. A special amortization plan must be requested which has debt service payments that are increased by the additional net income generated during the term of the abatement. When processing a short term or variable abatement, the full amount of the property taxes must be estimated and included in the total project expenses on Form HUD-92264 as if there were no abatement. The additional debt service carry resulting from the abatement must be calculated on line I, Criteria 5 of HUD-92264-A.

If Criteria 5, "Amount Based on Debt Service Ratio" is not the controlling criterion, short term or variable abatements cannot be used to secure additional mortgage proceeds. Also, the appraiser must not include extra value associated with short-term abatement in either the estimate of land value, the "As Is" value for substantial rehabilitation or the "As Repaired" value for existing projects, and it may not be included in Criterion 3.

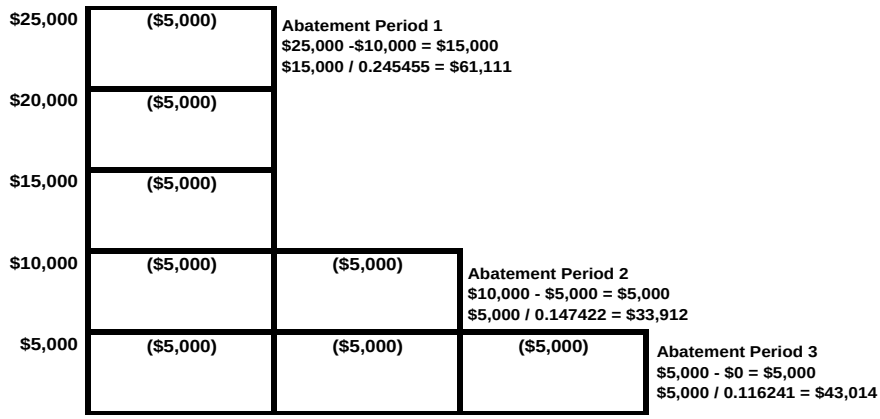
1. Short Term Abatements: Assume that Property A has been awarded a 5-year tax abatement of $5,000/year and the interest rate on the insured loan is quoted at 7.5% and the MIP is 0.5%. The amount of additional mortgage is calculated by dividing the annual abatement, $5,000 by the applicable debt service rate (P, I, and MIP). In this example the debt service rate is 0.245455383.

   $5,000 / .245455383 = $20,370

   Additional mortgage amount. The mortgage amount based upon debt service (Criteria 5 of HUD-92264-A) would be increased by $20,370 and a special amortization schedule would be required with a debt service payment that is $5,000/year greater in years 1 through 5.

2. Variable Abatements: Variable tax abatements are more complex to quantify, but are essentially calculated in the same manner. Assume that Property B has been awarded 15-year tax abatement. In years 1 through 5, the abatement is $25,000; in years 6 through 10 the abatement is $10,000; and in years 11 through 15 the abated amount is $5,000. The interest rate on the insured loan is quoted at 7.5% and the MIP is .5%. The amount of

additional mortgage is calculated as the amount that could be fully amortized by the variable payments over the 15-year period based on the stated financing terms. The graph below illustrates the calculation.



When there are two or more abatement amounts and periods, and the amounts decline, the abatement amount for each period is found by subtracting the abatement amount of the next period. Period 1 will run for 5 years, Period 2 will run for 10 years, and Period 3 will run for 15 years. Because all three periods begin amortization at the same point in year 0, the amount of the abatement for the next period must be subtracted to avoid double counting.

(1) Abatement Period 1

$25,000 minus $10,000 (the amount of abatement in period 2) = $15,000 for 5 years. The debt service rate for a 5 year term at 7.5% interest with 5% MIP is 0.245455383. Dividing $15,000 by 0.245455383 indicates additional mortgage proceeds of $61,111 attributable to period 1.

(2) Abatement Period 2

$10,000 minus $5,000 (the amount of abatement in period 3) = $5,000 for 10 years. The debt service rate for a 10 year term at 7.5% interest with 0.5% MIP is 0.147442123. Dividing $5,000 by 0.147442123 indicates additional mortgage proceeds of $33,912 attributable to period 2.

(3) Abatement Period 3

$5,000 minus $0 (since there are no periods remaining) = $5,000 for 15 years. The debt service rate for a 15 year term at 7.5% interest with 0.5% MIP is 0.116241483. Dividing $5,000 by 0.116241483 indicates additional mortgage proceeds of $43,014 attributable to period 3.

(4) Adding the supportable mortgages from each of the abatement periods results in a total additional supportable mortgage of:

Period 1 = $ 61,111

Period 2 = $ 33,912
Period 3 = $ 43,014
Total = $138,037

The mortgage amount based on debt service, (Criteria 5 of HUD 92264-A) would be increased by $138,037 and a special amortization schedule would be required with a debt service payment that reflects $25,000 per year in years 1 through 5, $10,000 per year in years 6 through10, and $5,000 per year in years 11 through 15.

7.17 Project Based Section 8 and LIHTC Processing

A. For Section 223(f). The property must be evaluated under two scenarios: a) the "hypothetical market value" of the property without regard to any Section 8 project based subsidies, rent restrictions or LITHC, and b) a debt service analysis that considers all Section 8 project based subsidies and other low income rent restrictions must be performed. Two independent Section C rent schedules must be prepared, one for a hypothetical market rent estimate and one that recognizes all rent restrictions and subsidies.

1. Criteria 3 Market Value: The appraiser must ignore the Section 8 contract rents, tax exempt bond or LIHTC restricted rents when determining market value and the income to be capitalized for a determination of market value for the purposes of determining Section K, Form HUD-92264, and Criteria 3 Form HUD-92264-A Value. To be consistent, the appraiser must use a market capitalization rate and must assume market rents in the income approach to value. Note that the comparable sales approach to value must be completed without regard to Section 8 or LIHTC awards.

2. Criteria 5 Debt Service Analysis: In calculating net operating income to be used for Criteria 5 Debt Service, rent restrictions must be observed. For the Criteria 5 debt service analysis, the Line 6, Form HUD-92264-T rents must be used. This applies to projects receiving LIHTCs that may use either tax exempt bond or market-rate financing.

3. Form HUD-92264T for LIHTC projects without Section 8: Follow existing form instructions. Processing will be based upon the lesser of Lines 1, 4 or 5.

4. Form HUD-92264T for Section 8 Project Based Assistance without LIHTC:

   a. Enter the market rent by comparison on Line 1
   b. Enter Personal Benefit Expenses on Line 2
   c. Line 3 is Not Applicable
   d. Line 4 is Not Applicable
   e. Enter the Project Based Section 8 Contract Rent on Line 5
   f. Subtract Line 2 from Line 5 (if applicable)
   g. Process using the lesser of Line 1 or Line 5

5. Form HUD-92264T for Section 8 Project Based Assistance with LIHTC:

   The LIHTC rent must be recorded but is not used as a limiting criterion because the total income to the project is the LIHTC rent combined with the Section 8 rent, so that the actual amount of rental income to the project will be the Project Based Section 8 rent, as follows.

2 Bedroom Section 8 Contract Rent	$850/Month
2 Bedroom LIHTC Rent limit	$350/Month
Resident's Rent Obligation to Project:	$350/Month
Section 8 Payment to Project:	$500/Month
Total Income to Project	$850/Mont

B. Fee Income. If additional fees for project amenities are mandatory for all residents, the mandatory fee income from restricted units must be excluded from the calculation of net income. The mandatory fee income from non-restricted units may be included if these amenity fees are indicated by comparable properties in the market and it must be explained in the remarks section of Form HUD-92264.

C. Expenses/Fees: Properties with LIHTC restricted units will commonly have a higher operating expense ratio per unit than market rate properties, which may be due to increased administrative costs for tax credit compliance monitoring, performing resident income certifications and staffing to provide on-site resident services. Estimating operating expenses for projects that are to be funded through the sale of LIHTC, requires the analysis of LIHTC comparables if available, and consultation with other experts (i.e. appraisers and property managers) in the context of current market conditions which should consider the size of the project and unit mix. Utility expense unit rent adjustments in LIHTC projects may be estimated by the analysis of actual costs supplied by the developer, the utility company or by use of the Section 8 utility allowances.

   1. If the property has the same operating expenses under LIHTC or Project Based Section 8 operation as it would under market rate operation, enter expenses as usual.

   2. If a property has different expense needs as a subsidized property, the expenses used for Criteria 3 must be market rate expenses and the expenses used for Criteria 5 debt service shall be the actual expenses under its' proposed usage. This will insure that the Criteria 5 - debt service analysis of the HUD 92264a is calculated based on the actual estimate of the rent restricted NOI for the property.

   3. Audit Fee no Longer Recognized. With the elimination of the requirement for an audited cost certification for mortgage insurance transactions with LIHTC, assuming the ratio of loan proceeds to the actual cost of the project is less than 80 percent, the audit fee will no longer be recognized as an allowable cost in the Total Estimated Replacement Cost of Project, Section G line 66 Form HUD-92264.

D. Sections 220 and 221(d) Site Value and "As Is" Value:

The site value of land in new construction or the "As Is" value in substantial rehabilitation cases is to be estimated using a capitalization rate and property NOI as if the units and the property were unrestricted and market rate, without considering: a) any additional value that may be attributable to subsidies available to the project or any LIHTCs or other tax benefits the property will receive, or b) any value reduction due to any NOI or value limitations caused by regulatory agreements or affordability restrictions imposed by any subsidy program or tax regulation. This valuation methodology permits sponsors to acquire property at its market value for new construction or rehabilitation of affordable housing. The value attributable to the presence of LIHTCs diminishes over time and is not always freely transferable, and thus should not be taken into consideration.

E. Income Limits. The review appraiser must ascertain that the correct income limits are employed in calculating the maximum LIHTC rents and in completing Form HUD-92264-T. HERA modified HUD's income limit methodology for calendar years after 2008 to require HUD to increase applicable area median incomes by the amount area median incomes rise, even if the HUD-determined area median incomes would be frozen under HUD's 2007 and 2008 income limit methodology. For LIHTC, HERA defines area median income in rural areas as the greater of the area median income and the national non-metropolitan median income, effective for income determinations made after date of HERA enactment, as applicable only to 9 percent LIHTC developments.

Chapter 8

Mortgage Credit Underwriting and Processing Requirements

8.1 Major Duties and Responsibilities of HUD

Major Duties and Responsibilities of HUD

1. HUD will perform the following mortgage credit functions during the application underwriting and construction periods.
   a. During application underwriting:
      (1) Review the Lender's mortgage credit report(s) regarding the acceptability of the sponsor, borrower and its principals, and the contractor.
      (2) Perform the Active Partner Performance System (APPS) Electronic 2530 Previous Participation Certification Property Submission review approval.
      (3) Determine the maximum mortgage amount and other key terms of the loan.
      (4) Determine actual financial settlement requirements.
      (5) Review initial and final closing documents for compliance and acceptability.
   b. During the construction period:
      (1) Review and approve the Lender's proposed initial distribution of mortgage proceeds.
      (2) Approve construction change orders.
      (3) Review the borrower's cost certification based on HUD allowed costs.
      (4) Determine the final maximum insurable mortgage.
      (5) Review and approve the final distribution of mortgage proceeds.

8.2 Pre-application Processing

A. Exhibits
   1. Lender's Underwriting Narrative (see Chapter 11)
   2. Form HUD-92013 Application for Multi-Family Housing Project
   3. If applicable, Form HUD-3433, Request for Preliminary Determination as Nonprofit Sponsor and/or Borrower and supplemental documentation

4. Form HUD-2530, Previous Participation Certification or Active Partner Performance System (APPS) Participant Certification page (participant signature page with submission id number). Either the HUD-2530 or the Electronic 2530 (E-2530) Participant Certification page may now be included as an exhibit as early as the pre-application stage of processing. Once the pre-application is assigned an FHA number, the participant can create the APPS E-2530 Property Submission for electronic 2530 approval. For applications that do not require a Pre-application stage, the 2530 Property Submission can begin once the application for Firm Commitment is assigned an FHA number.
5. Borrower and Development Team resumes, summary of sponsor's financial and credit information, and a basic organizational chart.

B. Mortgage Credit Duties and Responsibilities of the Lender's Underwriter

1. Determine general and financial acceptability of proposed sponsor/borrower and Development Team members.

C. Duties of HUD

1. Perform the electronic 2530 review and approval process.
2. Review Lender's preliminary analysis and recommendation about the Development Team's financial and general ability and creditworthiness.
3. Previous participation certification procedure concerns the past, present, and prospective performance and business practices of applicants undergoing administrative and underwriting reviews. HUD-2530 is not a substitute for processing as to project acceptability, credit capacity, or competency and the fact that HUD-2530 approval is granted is not assurance that the Department will grant final approval of the proposal or application.

8.3 Firm Commitment Processing – Determining Acceptability of the Borrower, Manager, and General Contractor

A. In General

A key component of the underwriting process is to assess the borrower's ability to manage the development, construction, completion, and successful lease-up of the property. The underwriting of multifamily projects involves evaluating the character, ability and financial condition of the sponsor, borrower and its principals, a property management company and the general contractor. The Lender's Underwriter must:

1. Identify the borrower and its principal or individuals.
2. Analyze the credit worthiness of the sponsors, the borrower entity, if formed, and it principals, individuals and the contractor.
3. Analyze the borrower and contractors experience record.
4. Determine the financial capability of the borrower and the general contractor.

5. The Lender's mortgage credit review must include:

   a. The balance sheets for all principals, and in addition to other relevant schedules, contain a Schedule of Real Estate Owned and a Schedule of Mortgage Debt of mortgages with maturity dates in the next 5 years or for properties which are troubled assets. A troubled asset is one that has or is likely to default on its mortgage obligations, or have significant financial management or operational problems.

      In each case the Lender will need to use its judgment as to how far back in a period of time they should review applicable data. Character is best demonstrated during periods of economic distress and so looking back at least through a complete business cycle is important. Any material credit problems in the last 2 to 5 years is very problematic and will typically (though not always) result in an application rejection. Events that occurred before that period if, for example more than 15 or 20 years have passed, would not have as material an impact on credit worthiness but may still be relevant. The Lender should consider this in the analysis and credit approval decision.

   b. The creditworthiness of all principals with a written analysis of their financial position and contingent liabilities, particularly all mortgage debt with near or intermediate term balloon payments (i.e. within the next 5 years forward).

   c. An analysis of the various properties' net operating income, outstanding indebtedness, cash flow and valuation estimates etc. The analysis must detail and support the Lender's assessment of the likelihood of the borrower's successfully refinancing projects with maturing balloon debt, assuming current capital markets conditions and current availability of alternative long term financing sources.

   d. An analysis that reconciles the data and concludes the borrower's creditworthiness. The analysis should give particular attention to principals with a history or anticipated incidence of adverse credit actions including (but not limited to) bankruptcies, foreclosures or a pattern of renegotiating debt.

   e. A financing plan for any shortfall or anticipated lack of available credit should be provided. Include both conventional financing and other FHA insured loans in this analysis.

   f. An analysis of large non-profit entities and large for-profit owners with large portfolios and audited summary financial statements. Such audited summary statements may be relied upon for the analysis. Generally, it will be sufficient for the Lender to provide summary data, including a description of exposure to maturing debt obligations, and a detailed listing and analysis of troubled projects, including those with recent or anticipated defaults or other material adverse actions.

6. Perform the U.S. Patriot Act required by the Office of Foreign Assets Control (OFAC)/Terrorism for checks and verifications on principals. These checks must be completed and documented at the time of Initial Endorsement, whether or not the Lender is a regulated financial institution. The OFAC is not part of MF Hub/PCs review. OFAC requirements are administered by the Department of the Treasury and Lenders should refer to the Treasury's website http://www.ustreas.gov/offices/enforcement/ofac, if you have any questions.

B. Exhibits

1. Data in the Application Multifamily Projects, Form HUD-92013 disclosing:
   a. Type of borrower entity.
   b. Interest rate, costs of issuance (if the project will be financed with tax-exempt or taxable bonds), financing fees and discounts to be charged.
   c. Names, addresses, telephone numbers and Social Security Numbers (SSN) or Employer Identification Numbers (EIN) for the sponsor, borrower, if formed, general contractor, attorney, architect and any consultant, if any is providing services beyond brokering the loan. NOTE: Providing the SSN/EIN is mandatory for the sponsor, borrower and their principals; however, this information is voluntary for all other participants.
   d. Sources of funds for the borrower entity.
2. Current resumes of the sponsor, borrower and its key principals, and the general contractor.
3. Participants must register using Form HUD-2530, Previous Participation Certification or APPS Participant Certification, for individuals, organizations and corporations.
4. Form HUD-92013 Supp, listing bank and trade references for all sponsors, the borrower, each principal of the borrower, and the general contractor along with disclosure of prior legal action, outstanding delinquent federal debt, and SSN or EIN, whichever is applicable.
5. A Fannie Mae Form 1006, Request for Verification of Deposit, for each bank reference included on Form HUD-92013 Supp.
6. Any Grant, Secondary Loan Commitment, and/or Tax Credit Allocation and Equity Investment Commitment letter (if applicable).
7. A listing from all sponsors, the borrower, all principals of the borrower entity and the general contractor of all business concerns in which these entities serve as a:
   a. general partner;
   b. limited partner with a 25% or greater interest;
   c. stockholder with a 10% or greater interest; or
   d. corporate officer.
8. A statement whether an identity of interest exists between the borrower and the general contractor, and/or architect.
9. Credit reports for all principals, current within 30 days of the application date.
10. Evidence of site control (valid option, purchase agreement or documentation proving ownership) and the date of the last arms-length transaction and price.
11. Certifications from the sponsor, the borrower entity, each principal and the general contractor, which authorize the release of banking and credit information. A certification similar to the following is required:

    "To Whom It May Concern:

    Please be advised that the undersigned, as (borrower/a principal sponsor/general contractor), hereby consents to the release of any banking and credit information in connection with the loan application for the construction of _____(project name)_____ to the

_____, Mortgagee, U.S. Department of Housing and Urban Development, and Delegated Processor or any Technical Discipline Contractor contracted by HUD to process this application.

By: _____ Date _____".

C. Identifying Principal Ownership Interest

1. There are numerous ways for investors to own an interest in real property. Each of these forms of ownership and level of involvement provides the investor with different capabilities and limitations in making a profit from the property. If the borrower or sponsor has a complex or layered organizational structure, review the structure and identify the controlling individuals or entities. Confirm that the borrower/ sponsor is legally organized in a manner that meets HUD requirements for owning and managing a property and consider any difficulties or increased risk that the organizational structure might pose in the event of default or foreclosure. All principals that meet the ownership and control standards in the previous participation regulation must register in the APPS/2530 system and are subject to the disclosure and certification requirements about bankruptcy, judgments, pending litigation and delinquent federal debt. Those principals with personal decision-making authority, active management roles, or who have a significant percentage of financial investment in the project are subject to more complete credit investigation. The Lender's Underwriter is responsible for identifying the principals and the extent of credit review required and appropriate.

   The additional mortgage credit scrutiny described here is intended to be forward looking and focused on the financial and managerial capabilities of those principals whose creditworthiness is essential for successful operation of the property being financed because they exercise decision making control over the property or they have a substantial ownership interest in the borrowing entity. The identification of such principals requires the exercise of a case by case underwriting judgment based on a review of the ownership structure of the borrowing entity.

2. Acceptable forms of property ownership in FHA insured transactions are:
   a. General Partnership (GP);
   b. Limited Partnership (LP);
   c. Corporation, C Corporation, S Corporation;
   d. Limited Liability Company (LLC);
   e. Trust (when the Borrower is a trust the duration of the trust must be equal to/longer than the term on the Note);
   f. Non-profit corporation; or
   g. Any other public or private single asset borrower entity, except ownership of the real estate as a natural person or as residents in common.

   Generally, foreign nationals and corporate entities may participate as principals, however, the single asset borrower entity must be registered in the United States in the State where their corporate office is located and at least one principal with operational decision-making authority must be a United States citizen.

Any combination of ownership forms can be used to establish a joint venture, for the purpose of jointly sharing the risks and the rewards by contributing the appropriate knowledge, skills or assets that are necessary to a successful development project. However, a single asset borrower entity is always required.

D. Identifying the Principals

1. Pursuant to 24 CFR Section 200.215(e), a principal is a public or private entity proposing to participate in a project as a sponsor, owner, prime contractor, etc. The principal's role can be one of actual participation in directing the activities and affairs of the borrower entity or involvement in decision-making, or one of inactive participation where an ownership interest has been acquired. All principals must be identified and analyzed based on their credit, experience, and financial histories.

   a. "Principals" for purposes of previous participation, credit and financial investigations are:

      (1) Any affiliate of the principals or principals of the borrower entity. If the principal is a partnership, all general partners and each limited partner having a 25% or greater interest in the partnership. If the principal is a public or private corporation or governmental entity; all operating officers; President, Vice-President, Secretary and Treasurer and any other executive officers who are directly responsible to the Board of Directors, or the equivalent thereof; all the directors and each stockholder having a 10% or greater interest.

      (2) Any principal who is an LLC and all managing members and all members with a 25% or greater interest in the LLC. A member is an owner of the LLC and is similar to a stockholder in a corporation or a limited partnership. A manager is a person chosen by the members to manage the LLC, which is similar to a director of a corporation or GP. A manager can also be a member.

      (3) General contractors;

      (4) Management agents; (Note: A financial and credit analysis is not required unless they meet the sponsor and owner criteria in Section 8.3 D (1) above.)

      (5) Packagers, consultants and other persons or organizations hired to furnish advisory services in project financing, construction or operation and the related HUD requirements, services may be included to select and negotiate contracts with contractors, architects, attorney or managing agents, secure financing; and

      (6) Architects and attorneys who have any interest in the project other than an arms-length fee arrangement for professional services. (Note: A financial and credit analysis is not required unless they meet the sponsor and owner criteria in Section 8.3.D (1) above.)

   b. Who is <u>not</u> a Principal for purposes of 2530, credit and financial investigations:

      (1) Stockholders with less than 10% interest in a corporation;

      (2) Limited partners with less than 25% interest in the partnership;

      (3) Attorneys and architects with only an arms-length fee arrangement for services;

      (4) Minor corporate officers;

(5) Sub-contractors;

(6) Brokers whose services are limited to referring the loan to a Lender and presenting information on behalf of the Borrower (i.e. that fall short of consultant or packing servicers);

(7) Public Housing Agencies/ Authorities;

(8) Members of non-profit Boards of Directors who are not officers as stated in Section 8.3.D above and have no active decision making authority and no active management role over the project being financed;

(9) Officers of passive investors (e.g. pass-through/ shell company, tax credit investor or syndicator); and

(10) Parties whose sole interest is that of purchaser or owner of less than five individual unit(s) in the same condominium or cooperative development; and parties whose sole interest is that of a resident.

(11) Tax credit investor partners who are Limited Liability Corporate Investors (LLCI) are exempt from the APPS/2530 review in accordance with Section 2(2) of the Preservation Approval Process Improvement Act of 2007.

E. The Credit Investigation

1. Lenders require credit reports or credit histories as a means of validating and cross checking information received from the borrower in the financial statements and application forms. Credit reports give a picture of the borrower's payment history and financial interactions with its creditors and allow the underwriter to make sound conclusions about the borrower's credit worthiness. They also allow the Lender to reconcile any significant contradictions between the financial statements and the credit report.
2. A commercial credit report for a business or a residential mortgage credit report (RMCR) for individuals must be current within 60 days of the application acceptance date and HUD may require updated reports during processing. Credit reports are required on:
   a. All sponsors;
   b. The borrower entity, if formed before submission of application;
   c. Principals of the borrower defined in Section 8.3 D.1.a. (1):

      NOTE: If a principal is a business entity (i.e. corporation, partnership, limited partnership) with an operating history, a credit report is required only on the business firm not the owners or tax partners of the firm.
3. Business concerns listed in Section 8.3.B.7 require credit reports on:
   a. All businesses with a pending judgment(s), legal action or suit or bankruptcy claim;
   b. 10% or more of the sponsor's other business ventures as selected by the mortgagee.
4. The general contractor.
5. The housing consultant, if applicable for nonprofit transactions.
6. A credit review of members of public and nonprofit boards of directors is not required unless the board member is also a board officer with decision-making role over the property.

F. Lender's Review of the Credit Report

1. All information obtained from credit reports and histories should be compared to the financial statements provided by the relevant borrower or principal(s). Any contradictory information should lead to further inquiry until the evidence shows a consistent and complete picture.
2. Make reasonable inquiries to determine if the applicant or any principal is in default on any federal debt, i.e., direct loans; HUD insured loans, student loans, Small Business Administration loans or judgment liens against the property for a debt owed to the federal government.
3. Determine if there is incomplete information or if there are inconsistencies or discrepancies between the information included on the financial statements and in the credit reports and resolve those inconsistencies or discrepancies.
4. Investigate any adverse credit information that appears on the credit report or which becomes known from making inquiries of bank and trade references and of other HUD offices. Require a written explanation of any late payments, actions, judgments or derogatory information.

G. Delinquent Federal Debt

1. When delinquent federal debt exits, the Lender must include as part of the required application exhibits:
   a. A detailed written explanation from any applicant or principal with a prior federal default or claim or whose credit report and financial statements contain conflicting or adverse information.
   b. A letter from the affected agency, on agency letterhead and signed by an officer, stating the delinquent federal debt is current or satisfactory arrangements for repayments have been made.
   c. The Lender's reason(s) for recommendation of the applicant, which may be included in the Lender's report described in Section 8.15.

H. Trade and Credit References

1. In addition to the credit report, the Lender must make inquiries of banks and trade references that are disclosed on the Form HUD-92013 Supp.
2. For bank inquiries, HUD relies on the completed Fannie Mae Form 1006, Request for Verification of Deposit. Obtain verification of deposit for each bank reference listed on Form HUD-92013 Supp and the participant's financial statements. Such bank references must include a sampling of mortgage payment histories and must confirm the character, business acumen, expertise and timeliness of the borrower and sponsor in meeting their business obligations.
3. Written inquiries of trade references should include a copy of the certification authorizing the release of credit information.
4. Do not require verifications of deposit on officers of a nonprofit corporation and officers of a profit-motivated corporation that have no ownership interest in the corporation and are not being relied upon for financial capacity. However, a general written inquiry to the bank about its experience with the corporation is required.

5. In addition to the formal documents and credit investigation described above, the Lender's Underwriter must conduct and describe the results of a thorough internet search of each principal and determine if there are any citations which raise concerns about credit worthiness.

I. Rejection Because of Unacceptable Credit

1. The Lender's professional judgment is required in approving or rejecting principals on the basis of creditworthiness.
2. Consider the principal a credit rejection if:
   a. The credit investigation evidences that the principal has a history of not repaying creditors in a timely manner or lacks liquidity.
   b. Delinquent federal debt has not been resolved or satisfactory arrangements made for repayment.
   c. There are judgments or actions against the party, which:
      (1) Could significantly impact upon the financial position of the individual/ firm or corporation.
      (2) Result in a determination that the individual/firm or corporation is an unacceptable credit risk.
   d. They are insolvent or are the subject of a pending bankruptcy or insolvency proceeding at the time of application, Firm Commitment, or at the time of loan closing.
   e. An REO Schedule shows unacceptable contingent liabilities or refinance risk that could destabilize the principals or distressed real estate that could materially impact their financial position.

J. Analyzing the Borrower's and Contractor's Previous Experience:

1. The Lender's underwriter must evaluate the resume of the principal(s). The principal must have positive experience and qualifications in developing, owning or building similar multifamily properties. Pay particular attention to:
   a. Type and size of previous multifamily projects and assess whether their requisite business experience shows that they are able to operate and manage a multifamily property of the size and complexity of the subject throughout the term of the mortgage. For borrowers on a property receiving LIHTC or other forms of subsidy such as Section 8 rental assistance, the Lender must ensure that the borrower has demonstrated experience in owning comparable regulated and subsidized properties and assess their handling of any adverse circumstances.
   b. Geographic area of business involvement;
   c. Length of time of involvement with development, ownership and operation of multifamily properties; and
   d. Past roles performed in the multifamily business.
2. Each resume should demonstrate the level of experience needed to successfully complete the development of the project. Identify new borrowers and sponsors whose primary business is

not real estate, have little multifamily experience or are new to a particular market. It may be necessary to inspect a sample of each borrower's real estate holdings to determine the quality of the assets and management of each borrower's existing portfolio. Explain any identified risks in their existing portfolios.

3. Require the addition of members to the development team if necessary to satisfy the experience requirements.

K. Principals with greater than $250,000,000 of outstanding FHA insured debt.

The Lender must perform a preliminary but thorough mortgage credit review and obtain HUD approval before submission of the application in cases where principals have greater than $250,000,000 of outstanding FHA insured debt (do not adjust for a principal's fractional ownership percentage). Based on the Lender's review of the principal's Schedule of Real Estate Owned, the Lender must identify principals that exceed the $250,000,000 threshold (not including Housing Finance Agency or Government Sponsored Enterprise risk sharing loans). Lenders will need HUD pre-approval before such principals or borrowers may apply for additional insurance commitments. The Lender's presentation to the Hub/PC must be approved by HQ Office of Multifamily Housing Development and must address the following items:

1. An analysis of the borrower's financial strength, credit history and experience.
2. An account of al insured and conventional debt on the REO schedule.
3. An explanation of mortgage debt, e.g. type, maturity, age, interest rate.
4. A full review and analysis of the operating performance and physical condition of the principal's existing insured properties.
5. An analysis and projection of the borrower's cash flow and liquidity for the estimated period of time required for proposed insured projects to achieve sustaining occupancy.
6. Previous Participation, HUD-2530.

NOTE: HUD will issue further guidance on the policies and procedures to follow when implementing this Section in a future notice.

8.4 Firm Commitment Processing Financial Statements

A. Introduction

1. Financial statements give a picture of the financial position of an individual/company at a point in time and provide historical information for measuring and evaluating the financial performance of a principal/firm and provide advance warning of financial problems.
2. The financial statement should be reviewed to determine if the sponsors, the borrower and/or the principals of the borrower have the financial capacity to develop, build and complete the project and whether the general contractor has the ability to deliver the project based on:
   a. Past financial condition;
   b. Present liquidity; and
   c. Projecting future financial capacity.

3. Complete the financial analysis to determine the amounts available for investment in the project by performing an analysis of working capital. Working capital is the difference between current assets and current liabilities and is used to purchase assets, pay off debt and make up deficits from operations. The financial analysis also determines which non-pledged, unsecured assets can be readily hypothecated to produce the required investment.

4. See Appendix 8D for instructions on how to correctly analyze financial statements when determining the financial capability of the Borrower, Sponsor, General Contractor and/or Manager of a LLC.

5. Real Estate Owned (REO) Schedule and Mortgage Debt Schedule. The purpose of requiring the REO and Mortgage Debt Schedules is to determine a principal's exposure to risk associated with real estate (e.g. multifamily, assisted living, new construction verses stabilized properties, commercial, office, undeveloped land, etc.). Generally, the REO Schedule lends credibility to asset values reported on the principal's financial statements by requiring detailed information on each real estate asset. It serves as a cross-check to the financial statements. The mortgage debt schedule should include loans that are maturing, or if floating rate debt have resets, within the next 5 years. Other debt that has a material impact on the principals' creditworthiness should be included as well (e.g. if they are in default or are likely to have problems with a loan over the next few years.)

   a. The requirements detailed in Section 8.4.B below, apply to those principals identified in Section 8.3.D above. These are principals who are actively involved in property operating decisions or are significant financial investors as identified in the borrower entity's organization structure. The Lender's Underwriter must determine which principals have control of the single asset entity and the property, and must assess their financial stability and how it will impact the risk to FHA, and must review their financial statements along with these schedules. Also, the Underwriter needs to analyze and disclose to HUD as part of their recommendation, any interests that do not rise to that level, but nevertheless have a material impact on the creditworthiness of the proposed borrower or its principals.

   b. If a tax credit syndicator is identified, the Lender's Underwriter will also need to provide a brief overview and analyses of the entity. Typically a tax credit syndicator is an investor intermediary with only a limited ongoing obligation to LIHTC rental properties. Accordingly an REO schedule is not required for tax credit syndicators or investors. However, the syndicator's liquidity, track record, asset management and monitoring capability and ability to perform on its commitment to provide equity to the borrower after Initial Endorsement is a material issue for mortgage credit analysis of the tax credit investor/LP.

   c. The Lender can present the REO and mortgage debt schedule in whatever format they wish so long as it contains the information covered in Section 8.4.B.2.d and any other sufficient information to present their underwriting analysis and conclusions. Typically the format is a spreadsheet accompanied by a summary description of each project's analysis. When the REO schedule differs from the financial statements, if the differences are material and not minor variations arising from timing of statements, or changes in principal balances, etc. then the Lender should investigate, reconcile and explain the differences.

B. Exhibits

The sponsor, borrower, (if fully capitalized), and general contractor must furnish current financial statements with supporting schedules as part of the application for commitment processing.

1. Individuals must submit either:
   a. Personal Financial and Credit Statement, Form HUD-92417:
      (1) The spouse of married sponsors or principals must also sign the form.
      (2) If a spouse's signature cannot be obtained, the principal must prepare the form reflecting only those assets that are solely in their name and any liability, including those joint liabilities, for which they have any responsibility.
   b. A substitute statement, which contains at a minimum the information contained on Form HUD-92417. This form must contain the following certification and criminal warning:
      (1) I HEREBY CERTIFY that the foregoing figures and statements contained herein submitted by me as agent of the borrower [owner] for the purpose of obtaining mortgage insurance under the National Housing Act are true and give a correct showing of _____'s (Name of borrower or owner) financial position as of _____ (date of financial statement).
      (2) Signed this ____ day of _____, 20___. Signature of authorized agent with name printed or typed under signature _____.
      (3) Warning – HUD will prosecute false claims and statements. Conviction may result in criminal and/or civil penalties. (18 U.S.C. 1001, 1010, 1012; 31 U.S.C. 3729, 3802)

      For married individuals, the spouse also must sign certification.
2. Business entities must submit the following separate statements and supporting documents for the last 3 years or the length of their existence. If less than 3 years, an authorized officer of the organization must provide the statements and supporting documents with a signed statement that there has been no material adverse change since the date of the statements.
   a. Balance Sheet which:
      (1) Provides a breakdown of current and non-current assets; a list of all other assets including the market value of each asset, the basis for calculating value (for real estate owned assets this will be shown on the schedule of real estate), and any notes receivable from related entities;
      (2) Identifies restricted and non-restricted funds;
      (3) Provides a breakdown of current and non-current liabilities; identifies the current portion of long-term debt; contingent liabilities, including debts under secured or unsecured lines of credit or letters of credit, personal guaranties, obligations to limited partnerships and other obligations payable in the future, including the amount and duration of the obligation; and
      (4) Lists details of any factors that may materially affect the borrower's or sponsors financial position now or during the term of the mortgage.
   b. Income and Expense Statement that reflects:
      (1) Income from normal operations;

(2) Investment income;

(3) Other income; and

(4) Total expenses.

c. If the financial statements are audited, a Statement of Changes in Financial Position or if a fund accounting system is used, a Statement of Changes in Fund Balance, and all notes.

d. Supporting Schedules:

(1) An Aging Schedule of Accounts Receivable that provides the name, type of account (trade, affiliate, employee, relative or other), payment terms, amount and aging information.

(2) An Aging Schedule of Notes Receivable that provides the name, type of account, payment terms, maturity date, current portion (due within 1 year or one operating cycle of the business, whichever is less), past due amounts and non-current amounts.

(3) Schedule of Pledged Assets, if applicable. Identify the pledged asset, the amount pledged and the offsetting liability.

(4) Schedule of Marketable Securities that provides: name, number of shares, current market values as of the date of the statement, and the exchange where the shares are listed.

(5) Schedule of Accounts Payable that provides: name, type of account (trade, affiliate, employee, relative or other), payment terms, amount and aging information.

(6) Schedule of Notes and Mortgages Payable that provides: name, type of account, payment terms, maturity date, current portion (due within 1 year or one operating cycle of the business, whichever is less), past due amounts and non-current amount.

(7) Schedule of Legal Proceedings, if applicable.

(8) In addition to the applicable schedules in the above paragraphs, general contracting firms must submit a schedule of jobs (work) in progress that identifies the:

(a) Original contract price;

(b) Construction start date;

(c) Construction completion date; and

(d) Percentage of completion.

(9) REO schedule that provides the following information for each physical property listed:

A. borrower/ principal's name

B. property name and address

C. type of property and number of units

D. property acquisition date

E. ownership role and interest

F. percent of current occupancy

G. annual net operating income

H. present market value

I. existing mortgages, liens and dates

J. interest rate and dates

K. sum of existing amount of mortgages and liens

L. current property equity

M. annual effective gross rental and commercial income (after deducting concessions and vacancy loss)

N. annual operating expenses

O. annual debt service

P. debt service coverage ratio

Q. pending judgments, legal suits/actions or bankruptcy against the property.

(10) A Schedule of Mortgage Debt is applicable only when the event of mortgage maturity is in the next five (5) years or the property is a troubled asset. Provide the following for each property listed:

- name of creditor/ lien holder
- type of debt (e.g. FHA mortgage, conventional mortgage, bridge loan, balloon)
- original mortgage amount or debt amount and origination date
- interest rate and origination date (i.e. fixed, fixed bonds, variable, etc.)
- unpaid principal balance or current debt amount and origination date
- maturity dates for all debt
- monthly payment
- balloon payment
- collateral (describe the security type for repayment of the mortgage or debt)
- status of debt as current or delinquent

e. Combined or consolidated financial statement(s), if applicable,

f. Other financial data necessary to determine the financial responsibility and capacity of the sponsorship or general contractor,

g. The certification signed and dated by an authorized official of the company. The certifications must reference the name of the business and the date of the financial statement(s).

3. Section 223(f) Project Financial Statements.

The proposed borrower must submit:

(1) the last 3 fiscal years financial statements on the project and if more than 3 months have expired since the closing date of the financial statements, a year-to-date balance sheet and operating statement,

(2) copies of the most recent insurance and property tax bills, and

(3) 3 years of tax returns for the property or borrowing entity.

If the statements are not audited, a CPA or IPA "reviewed" statement is required. "Audited," and "Reviewed," are defined professional standards for reports understood by CPAs. The intent of the requirement is to obtain an independent (non Identity of Interest) professional review of the financial statements certified by the Owner. If the statements are audited by an independent CPA or IPA, no further review is needed to validate the statements.

b. For refinance applications, not less than the last fiscal year and any required year-to-date financial statements must be CPA or IPA reviewed. For this purpose "CPA reviewed" means a review by a Certified Public Accountant and "IPA reviewed" means a review by a Independent Public Accountant of the records and statements of the mortgagor including specifically:

(1) The property financial statement(s) for the period;

(2) Rent rolls for each month of the period;

(3) Bank statements for not less than the last 6 months of the period; and

(4) The mortgagors income tax return for the last fiscal year

(5) With reconciliations of rent rolls to financial statements and financial statements to normalized operations, cash receipts and tax returns.

c. There may be circumstances beyond the borrower's control where the required financial statements are not available because of loss by fire, arson, theft, flood event etc.

(1) The borrower must submit:

(a) Evidence satisfactory to the Lender that the financial statements are not obtainable; and

(b) Project financial statements that are available including an owner-certified balance sheet and operating statement. (See item c. below)

(c) In all cases, the borrower must submit the past 3 years of tax returns for the property and the borrower entity.

(2) Lender's case file must contain a statement from the borrower that explains why all the required records are not obtainable and a memorandum from the underwriter to the Hub or Program Center Director stating that he/she has evaluated the borrower's statement and agrees that the information is not available.

d. Any owner-certified financial statement or owner-certified balance sheet and operating statement must include certification and criminal warning found in Section 8.4.B.1.b.(3).

e. Past Due Payables and Past Due Project Liabilities. Past due accounts payable and outstanding liabilities for project operating expenses must be cleared and released, or otherwise fully resolved, before or at Initial Closing. Examples of such items include deferred management fees, over-due utility bills or real estate taxes, or trade payables. These items are not to be included in the eligible debt basis in the calculation of the cost of refinance/ acquisition. If the transaction does not involve a Transfer of Physical Assets (TPA), and if approved by the Hub Director, surplus cash notes may be established for

payables owed to a related entity. Accounts payable and outstanding liabilities that are not past due do not need to be resolved at or before closing.

C. Processing Financial Statements and Other Documents.

1. A current financial statement must be no more than 3 months old when Form HUD-92013 is submitted to the Lender for Firm Commitment review. The Lender must determine financial stability and financial strength, unless the borrower and sponsor is a public company with an investment grade credit rating. Exceptions:
   a. The credit investigation or other circumstances may warrant more current financial statements.
      (1) Assess the adequacy of each sponsor's liquidity and its ability to provide immediate and ongoing support to the property, as well as to any asset that is in financial difficulty. For those properties in financial difficulty, consider that property's strength as well as liquidity sources outside the property, such as the sponsor. The Lender must look for likely future events that may drain cash resources from the sponsor.
      (2) The Lender may include other sources of sponsor cash flow in the analysis, if the source and stability of the cash flow has been verified by reviewing historical tax returns. Do not include interest income from notes receivable, real estate investment income, dividend income and sponsor salaries.
   b. Audited or reviewed financial statements prepared by a CPA or IPA independent public accountant may be up to 1 year old. The audited or reviewed statements must be supplemented with updated interim financial statements and supporting documentation, which may be management-prepared, if more than 6 months have lapsed since the closing date of the audited statement.
2. A borrower entity with adequate capital must provide financial statements on the individual ownership interest(s). This borrower entity must be fully funded in an account in the name of the borrower entity.
3. A working capital determination is to be made for the borrower and the general contractor from a review of the financial statements. The net working capital is to be adjusted for the effect of contingent liabilities and the financial needs of other projects in the planning stage or under construction, adjusted by the percentage of completion.
4. Net worth in lieu of working capital occurs when existing assets can secure loans or lines of credit to cover the project's financial requirements and such loans or lines of credit are confirmed as being available, the underwriter should recommend approval based on "true net worth" rather than on working capital.
   a. Require the principal to provide a commitment letter from a lending institution that states:
      (1) The rate, amount, term and conditions, if any, of the loan that the lending institution is willing to provide.
      (2) The date by which the commitment letter must be exercised; the date must extend at least to the anticipated date for initial endorsement.
      (3) The party that will be responsible for repayment of the loan or line of credit, if the commitment is exercised.

(a) Repayment may not be an obligation of the borrower entity.

(b) A certification indicating that the lending institution will not make any claim against the mortgaged property, mortgage proceeds, any reserve or deposit required by HUD, or against the rents or other income from the mortgaged property for payment of the loan or line of credit. This certification must contain the criminal certification.

5. Funds provided by a parent company or affiliate of the sponsor. Require a certification from the Board of Directors or authorized agent that specifies the funds the parent company/affiliate will commit. Establish the availability of funds from the parent company/affiliate. Consider whether:
   a. Individual corporations have any excess operating capital.
   b. Laws under which they are incorporated or their banks permit:
      (1) Withdrawals, loans or advances to owners or sponsors.
      (2) Stock investment in affiliated corporations.
      (3) Guarantee of debts of associated corporations.
6. Letters of intent and letters of credit cannot be used to establish financial capability. At initial endorsement, however, letters of credit may be substituted for cash to set up many of the escrows required at initial and final endorsement, or during construction. If a borrower draws down cash at initial closing to satisfy escrow requirements, a letter of credit cannot be substituted to establish the same escrow requirements.
7. Ratings and requirements for bank issued letters of credit. When a letter of credit is permitted, the ratings and requirements for banks issuing letters of credit for all multifamily project escrows must meet the following GNMA criteria:
   a. Unconditional and irrevocable;
   b. Issued by a bank in a GNMA rated institution which are insured depository institutions, which can include FDIC or National Credit Union Administration, with a rating that is acceptable to HUD (refer to Chapter 16-8 and Chapter 31-15(B), MBS Guide 5500.3 Rev. 1, 10/01/09, for details);
   c. Is deposited into a non interest bearing account; the institution does not have to be fully insured by the United States of America;
   d. Valid and collectible; and
   e. Have a term that equals the period of the escrow or of the borrower's obligation and is acceptable to HUD.
   f. The format of the letter of credit must follow that in GNMA Handbook 5500.3, REV-1 Appendix VI-3;
   g. The Issuer must be named as beneficiary. The Issuer must execute, in blank, a Transfer of Letter of Credit using the format included in Appendix VI-3, the original of which must be filed with the document custodian; and
   h. Any substitute letter of credit or extension that changes the letter of credit number or any terms or conditions of the letter of credit will require a new execution in blank and filing of

a Transfer of Letter.

The requirements for depository institutions and deposit accounts are in found in the current GNMA MBS Guide for Issuers, 5500.3. It is available on GNMA's website at the following link. http://www.ginniemae.gov/guide/guidtoc.asp?subTitle=Issuers.

8. The Lender of record may not be the issuer of any letter of credit without prior written consent of the Hub Director. Such consent will only be granted on an exception basis with sufficient investigation about a potential conflict of interest. If a demand under any letter of credit is not met immediately, the Lender must provide the cash equivalent to the un-drawn balance of the letter of credit.

9. Lines of Credit. On an exception basis and with prior written consent of the Hub Director, existing lines of credit may be used to establish a portion of the principal's financial capability. With the Firm Commitment application, the Lender must have the principal provide a letter from a lending institution that confirms:

   a. The existence of the line of credit, original amount and available balance, repayment terms, and expiration date.

   b. The line of credit expiration date cannot occur prior to project completion.

10. Sponsor's Continuing Commitments.

    a. A written statement must be submitted from principals who are sponsors indicating the parameters of their financial commitment to and contractual relationship(s) with the borrower:

       (1) If the relationship is not intended to continue until the project reaches sustaining occupancy, the financial requirements have not been met.

       (2) Any sponsor not having an ownership interest in the borrower entity must also certify in writing the amount it will commit.

    b. The Firm Commitment will contain special conditions to ensure the contractual association of the sponsor to the project:

       (1) The condition must indicate that the withdrawal of any individual/firm relied on for financial capacity requires prior to HUD approval.

       (2) Identify the individuals/firms relied on for financial capacity. For confidentiality reasons, do not indicate their alphabetic designation or their dollar contribution listed on Form HUD-92264-A.

       (3) Indicate that the withdrawal of any individual/firm relied on for financial capacity could result in HUD declaring the Firm Commitment null and void.

    c. Require organizational documents reflecting such continuing contractual relationships.

    d. If there is a change in sponsorship of the individuals/firms relied on for financial capacity and the remaining principals do not demonstrate the capacity to meet the financial requirements of the project:

       (1) At any stage through Firm Commitment this is considered a significant deviation from the original proposal and a cause for rejection of an application.

(2) After the issuance of the Firm Commitment, but before Initial Endorsement occurs, this is considered a significant deviation from the application for which the commitment was issued and may be cause for declaring the Firm Commitment null and void.

11. Individuals are prohibited from submitting financial statements as a sponsor and then abandoning the project and the borrower after the Firm Commitment is issued. The Lender should require a certified statement from the sponsor stating their commitment to the project and specifying the amount of funds that will be reserved for contingent needs through Final Endorsement and sustaining occupancy.

12. The submission of a financial statement that is used to influence Federal Officials concerning a mortgage insurance risk determination when the sponsor does not plan a continuing relationship with the borrower could result in appropriate sanctions being taken against the sponsor including suspension or debarment.

13. General Contractor with Adequate Capital: The general contractor's adjusted working capital position should equal 5% or more of the estimated construction contract.

    a. The instructions for hypothecation of fixed assets may be applied if the general contractor does not have an acceptable working capital position.

    b. The general contractor's ability to obtain a performance-payment bond does not negate or lesson this requirement.

    c. Adjust the working capital for projects in construction.

    d. If the general contractor does not have an acceptable working capital position or sufficient fixed assets that can be hypothecated, a joint venture may be established with a financially stronger general contractor provided these firms' combined working capital equals at least 5% of all construction contract amounts for projects in construction and development.

    e. Waiver of the working capital requirement is reserved to Hub Directors, and will only be considered when there are specific strongly supported mitigating factors.

14. In the case of LIHTC, Historic Tax Credit or New Market Tax Credits transactions, the application may include a *Letter of Commitment* to fund the required equity from a tax credit equity syndicator or investor. This *Letter of Commitment* must specify the equity amount, pay-in schedule and other relevant details such as conditional benchmarks so that HUD and the Lender can ensure sufficient equity in a manner that meets HUD's requirements. The Lender may also make the determination to require additional documentation (e.g. financial statements, etc.) of a syndicator or investor to demonstrate their ability to make the future equity installments. See Chapter 14 for further guidance on underwriting an application with tax credits.

    Recognizing that the borrower or sponsor's financial capacity may be weaker in affordable housing transactions, the Lender should also focus on and evaluate the tax credit syndicator's or the direct investor's financial strength, experience, reputation and asset management capabilities, if they have the majority ownership interest in the borrower entity, as is addressed in Sections 8.3.D and 8.3.J. Evaluating the syndicator is important because investors expect syndicators to support transactions that have cash flow problems or replace nonperforming general partners. In addition, the syndicator must typically assess the appropriate amounts of

reserves at both the property and fund levels and must perform certain asset management functions.

8.5 Term of Mortgage and Commencement of Amortization

A. For Sections 220, 221(d)(3), 221(d)(4), and 231 projects:

1. The term of the mortgage is the lesser of 75% of the estimated remaining economic life of the physical improvements or 40 years from the date of the first payment to principal.
   a. Express the mortgage term in whole or partial years.
   c. Express a partial year in months, for example 26 years, 3 months.
2. Amortization starts:
   a. For Insurance of Advances projects, no later than 4 months after the date of construction completion as estimated in the Firm Commitment.
   b. For Insurance Upon Completion project, the first day of the second month following the date of Final Endorsement.

B. For Section 207 pursuant to 223(f) projects:

1. The term of the mortgage shall not be less than 10 years, nor shall it exceed the lesser of 35 years or 75 percent of the estimated remaining economic life of the physical improvements.
   a. The mortgage term shall be the eligible number of whole or partial years between 10 and 35.
   b. Express a partial year in months, for example 26 years, 3 months.
2. Amortization starts on the first day of the second month following the date of the Initial/Final Endorsement of the mortgage for insurance.

8.6 Additional Firm Commitment Processing Exhibits

A. For Sections 220, 221(d)(3), 221(d)(4), 231, and 207 pursuant to 223(f) projects, include:

1. Underwriter's Narrative
2. Form HUD-92013, Application for Multifamily Housing Project
3. Form HUD-92264, Rental Housing Project Income Analysis and Appraisal
4. Form HUD-92264-A, Supplement to Project Analysis

8.7 Sections 220, 221(d) and 231 Firm Commitment Processing - Determining Mortgage Amounts, Cash Requirements and Related Items

A. Firm Commitment Processing.

1. New Construction Loan Limits. On a loan for new construction, the insurable loan amount is the lowest of four criteria on Form HUD-92264-A, Supplement to Project Analysis: the application amount, the cost amount, the statutory limits amount, and the debt service amount, which are described below. Refer to Chapter 3 Sections 3.5, 3.6, 3.7, or 3.8 for the applicable program required maximum loan ratios and the debt service coverage ratios needed to complete criteria for new construction and substantial rehabilitation firm applications.

   a. The Application amount.

   b. Amount Based on Value or Replacement Cost. The result of Lender's estimate of the replacement cost after completion, multiplied by the applicable percentage.

   c. Amount Based on Limitations Per Family Unit - Statutory Limits. An amount attributable to dwelling use, excluding land, not to exceed the per unit limits as adjusted by the High Cost Percentage (HCP) for the jurisdiction in which the project will be located, plus the percentage loan ratio noted in A.1 above, times the sum of costs not attributable to dwelling use (from Form HUD-92264 Section M Line 15) and the warranted price of the land (from Form HUD-92264 Section G Line 73a) (or the "as is" value of the building without the improvements if the transaction is a substantial rehabilitation loan, from Form HUD-92264-HCF Section H Line 38). See Appendix 8B for the HCP.

   d. Amount Based on Debt Service Limit. The loan amount supported by the applicable percentage of projects' estimated net income.

      The NOI used to support this mortgage criterion may be split into two or more income streams, for example to capitalize the savings from tax abatement or to recognize other revenue sources such as from an IRP decoupling.

      (1) That portion of the maximum mortgage supported by the tax abatement or other source of must be amortized over the same period as the additional NOI as available.

      (2) Any tax abatement must run with the real estate and not with the type of sponsorship if it will be recognized in the mortgage proceeds.

2. Substantial Rehabilitation Loan Limits. Amount of Loan – Rehabilitation under Section 220 and 221(d). (This includes only projects involving substantial rehabilitation or reconstruction.) The insurable loan amount is the lowest of four criteria on Form HUD-92264-A, Supplement to Project Analysis: the application amount, the cost amount, the statutory limits amount or the debt service amount, as described below. Refer to Sections 3.5, 3.6 or 3.8 for the applicable program required maximum loan ratios and the debt service coverage ratios needed to complete the criteria for substantial rehabilitation firm commitment applications.

a. The Application amount.

b. The Lender's estimate of the rehabilitation cost plus the fair market value of the land and existing improvements before rehabilitation, multiplied by the applicable percentages in Sections 3.5, 3.6 or 3.8.

c. Amount of Loan – Rehabilitation under Section 231. (Only for projects involving substantial rehabilitation or reconstruction.) The amount as permitted under the new construction program except the loan limitation is based on the estimate of value rather than the replacement cost. The insurable amount is the lowest of:

(1) The application amount;

(2) Property owned – 100% of the estimated cost of rehabilitation plus the lesser of:

(a) Principal amount of existing indebtedness against the property and closing charges, or

(b) For all borrowers, apply the amounts in Section 3.8, to calculate the Lender's estimated appraised value of the property before rehabilitation and closing charges less:

(i) Value of leased fee, if leasehold, and/or

(ii) Principal amount of special assessment.

(3) Property to be acquired – For all borrowers, apply the amounts in Chapter 3 Section 3.8 to calculate of the Lender's estimated current cost of rehabilitation/reconstruction plus the lesser of:

(a) Apply the amounts in Section 3.8 for all borrowers to calculate the actual purchase price of the property and closing charges, or

(b) For-profit borrowers, apply the amounts in Chapter 3 Section 3.8, of the Lender's estimated appraised value of the property before rehabilitation and closing charges and/or principal amount of special assessment.

3. Complete Criteria 11 for all Sections of the Act (SOA) when secondary financing applies so long as the SOA are not exempt by law from subsidy layering review.

Amount Based on Deduction of Grant(s), Loan(s), Tax Credit Equity and Gift(s) for Mortgageable Items.

100% Replacement Cost or Value* less the sum of all Grants/loans/gifts and Tax Credits.

*Project Replacement Cost applies to Section 221(d) and other Sections of the Act mortgages limited by replacement cost. Value applies to Section 223(f) and Section 231 substantial rehabilitation.

B. Insurance of Advances.

See Section 12.7 and Appendix 12 for processing instructions.

8.8 Section 223(f) Firm Commitment Processing - Determining Mortgage Amounts, Cash Requirements, and Related Items

A. Firm Commitment Processing for Section 207 pursuant to 223(f):

1. Amount of loan in a purchase transaction.

In a purchase transaction involving an arm's length sale, the mortgage may not exceed the lowest of 5 criteria on Form HUD-92264-A, Supplement to Project Analysis: the application amount, the cost amount, the statutory limits amount and the debt service amount. Refer to Chapter 3 Section 3.9 for the applicable maximum loan ratios and the debt service coverage ratios needed to complete criteria for a firm purchase application.

a. The Application amount.

b. Amount Based on Loan to Value Ratio. Refer to Chapter 3 Section 3.9 for ratios. These loan-to-values apply to both for-profit and nonprofit borrowers. (The amount based on value for Section 202 or 202/8 Direct Loan purchase transactions is 90%.)

c. Amount Based on Limitations Per Family Unit - Statutory Limits. The maximum per family unit limitation for new construction under Section 207 may be increased by the percentage of the HCP plus the percentage loan ratio noted in A.1.b, above, cost not attributable to dwelling use, from Section M Line 15 of the Form HUD-92264 and the "Warranted Price of Land." This corresponds to Section G Line 73a of Form HUD-92264, Multifamily Summary Appraisal Report.

NOTE: Per family unit limits may be increased the HCP. See Appendix 8B.

d. Amount Based on Debt Service. The loan amount supported by the applicable percentage of the projects' estimated net operating income (NOI). The mortgage may exceed this limit by capitalizing the savings from any tax abatement. In such cases, the net earnings estimate will not reflect that temporary tax abatement.

The NOI used to support this mortgage criterion may be split into two or more income streams, for example to capitalize the savings from tax abatement or to recognize other revenue sources such as from an IRP decoupling.

(1) That portion of the maximum mortgage supported by the tax abatement or other source of must be amortized over the same period as the additional NOI as available.

(2) Any tax abatement must run with the real estate and not with the type of sponsorship if it will be recognized in the mortgage proceeds.

e. Acquisition Cost. The applicable percentage from Chapter 3.Section 3.9 must be applied to the borrowers acquisition cost. Acquisition cost is defined as the sum of the items:

(1) Purchase price shown in the purchase agreement and determined allowable by the Lender.

(2) The Lender's estimate of repair cost, if any, provided such costs are paid by the borrower and are not included in the purchase price.

(3) The sum of reasonable financing charges, legal, organizational, and title and recording expenses paid by the borrower.

(4) Eligible discounts paid by the borrower at property acquisition.

NOTE: Any fees, discounts or other amounts paid by the seller for or on behalf of the purchaser must be reflected as a reduction to the acquisition cost.

(5) Eligible architect's fees, mechanical engineering fees, municipal inspection fees, HUD inspection fees, if applicable, and other fees as may be determined eligible by the Lender including the cost of Lender third party reports.

f. Complete Criteria 11 for all Sections of the Act (SOA) when secondary financing applies so long as the SOA are not exempt by law from subsidy layering review.

Amount based on Deduction of Grant(s), Loan(s), Tax Credit Equity and Gift(s) for Mortgageable Items. (Criteria 11)

100% Project Costs* less the sum of all grants/ loans/ gifts, tax credits for mortgageable items.

*Project Cost applies to Criteria 7 Line g and 10 Line g of Form HUD-92264-A under Section 223(f).

2. Amount of Loan in a Refinancing Transaction:

The subject loan will be the lesser of:

a. Amounts in Section 8.8.A.1., except e.

b. Cost to Refinance. An amount that equals the greater of the following:

(1) 80% of the Lender's estimate of the value of the project, or

(2) The cost to refinance the project, which is defined as the sum of:

(a) The amount needed to pay off the existing indebtedness as determined eligible by the Lender.

(b) The initial deposit to the Reserve for Replacements.

(c) The sum of reasonable financing charges, legal and organizational, and title and recording expenses paid by the borrower.

(d) The Lender’s estimate of repair cost, if any.

(e) Eligible discounts paid by the borrower.

(f) Eligible architect's fees, mechanical engineering fees, municipal inspection fees, HUD inspection fees, if applicable, and other fees as may be determined eligible by the Lender including the cost of Lender third party reports.

(g) Less the amount of any: Reserve escrow for replacement and/or major movable equipment that will be purchased as an asset of the project.

c. Release of Cash-Out / Equity from Loan Proceeds.

The maximum loan to value ratio for cash out refinances is 80%. One half (50%) of any cash out proceeds after funding any transaction (mortgageable) costs including the assurance of completion requirements, must be held in escrow by the Lender until the non-

critical repairs are completed and HUD approves the release. This is true whether or not there are non-critical repairs. See Section 8.13 for establishing cash-out/equity requirements.

B. Identity of Interest Purchase Transaction.

Refer to Section 13.16.

C. Determining Existing Indebtedness in a Refinancing Transaction.

Existing indebtedness in a refinancing transaction is defined as:

1. Outstanding mortgage(s) incurred in connection with the construction of the project or with capital improvements made to the property as confirmed by the current mortgagee. Use the pay-off letter which appears in Appendix 8C of this Guide.
2. Other recorded indebtedness such as mechanic's liens and tax liens provided they did not result from personal obligations of the borrower.
3. Unrecorded debt directly connected with the project supported by documentation from the borrower. If the indebtedness is not recorded, the borrower must provide the Lender with documentation, which unquestionably identifies the indebtedness with the project and are not the result of unpaid operational expense such as delinquent interest, accounts payable or deterred management fee. Examples are:
   a. Prepayment penalties on the mortgage.
   b. Indebtedness incurred in making significant betterments to the property.

   NOTE: Program penalties arising from the defeasance of tax-exempt and taxable bonds cannot be recognized. Similarly, the costs of settling prepayment penalties or yield maintenance fees associated with swaps or other derivatives (i.e. swap breakage fees) are not eligible to be included in the calculation of existing indebtedness.
4. Mezzanine Debt. Mezzanine debt may only be considered in the eligible basis for refinancing where there is no identity of interest between the principals and the Mezzanine Lender or any of its affiliates, or there is no identity of interest recognized for funding capital improvements. Mezzanine debt can be included in the eligible debt basis in a refinance if the loan documents associated with the mezzanine financing clearly identify the debt as directly funding the costs of the property and of any improvements.
5. Do not recognize indebtedness:
   a. Recently placed against the project to increase the mortgage or circumvent program intent. **NOTE**: "Recent indebtedness" for multifamily properties is defined as any debt incurred up to 1 year before application for mortgage insurance is made. However any/all recent debt not incurred as part of the acquisition or construction of the project or incurred for capital improvements made to the property is ineligible. Sufficient documentation must be provided in support of said debt being incurred on/for the project.
   b. Created by wrap mortgages
      (1) The borrower and Lender must give a detailed explanation of the purpose of the wrap and a documented accounting of the use and disbursement of the loan proceeds.

(2) The Lender may recognize loan proceeds used for capital improvements or project operations.

D. Reserve for Replacements.

The cost of an initial deposit to the Reserve for Replacements is eligible for inclusion in the maximum insurable mortgage.

1. Purchase Transaction.
   a. The purchase agreement must specify:
      (1) Whether or not the transfer includes as an asset of the project, Reserve Fund for Replacements, or other escrows.
      (2) Dollar amounts of escrow and/or items which the seller will pay on behalf of borrower, e.g., the operating deficit, discounts, initial deposit to the Reserve fund for Replacements.
   b. Apply existing Reserve Funds transferred as an asset of the project as a reduction of acquisition cost when computing Criterion 7 on Form HUD 92264-A.
2. Refinancing Transaction. The borrower must submit a list of escrows currently on deposit for the project:
   a. The escrow account and minimum Initial Deposit to the Reserve of Replacements must remain with the project.
   b. Apply funds currently on deposit in a Reserve for Replacements as a reduction of the cost of refinancing under criterion 10 on Form HUD 92264-A.

E. Discounts and/or Costs of Issuance associated with bond financing may be eligible for inclusion in the computation of Criteria 7 and 10. See Chapter 3 Section 3.9.S.

8.9 Secondary Financing

The amount, form, terms and conditions of any permitted secondary financing is based on the source of funding, as follows:

A. For all SOA, when the secondary financing is from a federal, state or local governmental source:
   1. Use Form HUD-92420M, Subordination Agreement; the subordinate loan be secured by a promissory note and mortgage lien as is prescribed by the governmental funding source and reviewed and approved by HUD.
   2. Secondary financing or grants lent to the property as a secondary loan may be used to cover up to 100% of the applicable SOA equity requirements.
   3. Secondary financing or grants lent to the property as a secondary loan may also be used to finance non-mortgageable costs, and when added to the HUD mortgage and required equity contribution, may exceed 100% of the project's Fair Market Value (FMV) or Replacement Cost.

4. Non-mortgageable costs (i.e. replacement cost items, not eligible for inclusion in the HUD insured loan) to be covered by governmental secondary loans, or grants lent to the property as a secondary loan, must be certified by the funding source to be reasonable and necessary to complete the project and that the project costs to be covered by the secondary financing are reasonable. Documentation to this effect must be included with the application submission.
5. The governmental secondary financing Lender must agree to and enter into a HUD prescribed form of Subordination Agreement that details the rights and legal relationship between the FHA insured first mortgage and the secondary financing loan.

B. Secondary Financing when the loan is from a private source.

1. Section 223(f).
   a. Secondary financing from a private lending source must be evidenced by unsecured promissory note, see descriptions below, and may not be secured by a lien on the property. The note may not be modified or altered in any manner without the written consent of HUD. A rider should be attached to the secondary financing note, a sample of which is found in the Multifamily Closing Guide.
   b. The secondary financing is permitted to cover a portion of the equity requirement under Section 223(f). The aggregate amount of the FHA insured first loan and the private secondary loan cannot exceed 92.5% of FMV. Therefore, the amount of a private loan may range from 7.5% of FMV (the difference between 85% and 92.5% of FMV) to a larger percentage if the mortgage criterion is lower than 85% of FMV controls. Secondary financing from private sources are not permitted under other SOA.
   c. When private secondary financing is combined with federal, state or local governmental agency secondary financing, as in paragraph A above, the aggregate amount of HUD insured first loan and the private secondary loan cannot exceed 92.5% of FMV. However the governmental loan, in aggregate with the HUD first and private second, may exceed the property's FMV. The addition of the governmental loan may result in total liens that exceed the property's FMV.
   d. Private secondary financing may be used to cover non-mortgageable costs in combination with equity or solely for one purpose or the other. Whatever option is decided upon, the aggregate of the HUD first and private second cannot exceed 92.5% of FMV.
   e. Non-mortgageable costs or non-HUD replacement cost items to be covered by secondary financing from private sources must be certified by the funding source to be reasonable and necessary to complete the project and that the project costs to be covered by the secondary financing are reasonable. Documentation to this effect must be included with the application submission.
   f. Mezzanine Financing. Mezzanine financing is provided by a private lending source and is usually secured by a pledge of partnership interests rather than by a secondary lien on the real estate. The existence and terms of all mezzanine debt must be fully disclosed to and approved by HUD during the application process. Any mezzanine debt that remains from a previous financing of the property is subject to the secondary financing guidance for private sources in this section. Repayment of mezzanine financing can only be made from surplus cash and the mezzanine loan cannot mature before the term of the FHA insured

loan. It must be shown that the projected surplus cash may be reasonably expected to pay the interest due on the mezzanine loan. The mezzanine loan interest rate typically will be higher than the rate of the first mortgage, but must be reasonably consistent with market rates for mezzanine debt and must not be so high a rate that it jeopardizes the ownership stability of the property or that the interest due cannot reasonably be expected to be repaid from surplus cash. Interest due or accruing on the mezzanine loan must be approved as reasonable by HUD.

Any transfer of an ownership interest in the borrower entity or in its principals to the mezzanine Lender in the event of nonpayment or a default on the mezzanine debt must have prior written approval by the HUD through the Transfer of Physical Assets (TPA) process or it will be invalid. The mezzanine Lender can exercise no enforcement remedies as against the real estate or as against the borrower entity during the term of the mezzanine loan.

2. New Construction/Substantial Rehabilitation Programs. Private secondary financing is not allowed under Section 221(d)(4) or other new construction/substantial rehabilitation first mortgage programs, except in cases where the FHA loan is less than 50% of the mortgageable cost. Seller financed secondary debt cases can be used for identity of interest transactions so long as the selling price of the land or building is not greater than the "as is" value.

C. Repayment of public or private secondary financing, including interest, must be soft and be made solely from 75% of available surplus cash. Include the following language in the soft note:

"*So long as the Secretary of Housing and Urban Development or his/her successors or assigns, are the insurers or holders of the first mortgage on (insert project name and FHA Project No.), payments due under this soft note shall be payable only from 75% of available surplus cash) said project, as the term surplus cash is defined in the Regulatory Agreement dated (insert date) between HUD and (insert name of borrower). The restriction on payment imposed by this paragraph shall not excuse any default caused by the failure of the maker to pay the indebtedness evidenced by this soft note*."

D. The borrower may secure a promissory note with a subordinate lien from a governmental agency against the property under the following conditions:

1. The Lender on the insured mortgage must consent to the placing of the subordinate lien and agree that its existence does not constitute a basis for default on the first mortgage.
2. There must be a simultaneous closing and same day recordation of the subordinate financing documents and the insured first mortgage loan documents.
3. The terms of the subordinate mortgage must be:
   a. Approved by the Field Counsel;
   b. Consistent with the terms of the insured surplus cash note, the first mortgage, the Regulatory Agreement and all HUD regulations and requirements.
   c. The subordinate mortgage shall not contain a cross default provision or any right of foreclosure before the termination of the FHA insured mortgage.
   d. The term of the subordinate mortgage must be extended, if:

(1) The Note matures, there are no surplus cash funds or residual receipts available for repayment and the first mortgage has not been repaid in full. (Distribution of residual receipts can only be approved by the terms of a written agreement between HUD and the owner.)

(2) HUD grants a deferment of amortization or forbearance that result in an extended maturity of the insured mortgage.

e. The subordinate mortgage must be assumable when a sale or transfer of physical assets occurs and the insured mortgage remains in place.

(1) The holder of the subordinate mortgage cannot require that more than 75% of the net proceeds of the sale or transfer be applied to the reduction of the loan.

(2) For these instructions, net proceeds are the funds available to the original borrower after:

(a) Correcting any monetary or covenant default on the first mortgage.

(b) Making:

(i) Required contributions to any reserve funds.

(ii) Needed improvements to the property as evidenced by HUD's annual inspection reports.

f. The subordinate mortgage must automatically terminate if HUD acquires title to the project by a deed in lieu of foreclosure.

g. Only 75% of surplus cash can be pledged to the repayment of the subordinate loan(s).

h. Terms of unsecured private Promissory Notes must reflect those provisions found in: Form HUD-91710M, Residual Receipts Note (Nonprofit Mortgagor), Form HUD-91712, or Residual Receipts Note (Limited Dividend Mortgagor), or the Form HUD-92223M, Surplus Cash Note [applicable to for-profit mortgagors; formally called Promissory Note], depending upon type of mortgagor, or must include the terms set forth in the Secondary Financing Rider, refer to the Multifamily Program Closing Guide, Part 5.

(1) Form HUD-91710M, Residual Receipts Note (for Nonprofit Mortgagors) and Form HUD-91712M, Residual Receipts Note (for Limited Dividend Mortgagors).

(a) Principal and interest shall be due and payable on or after the maturity date of the HUD-insured mortgage.

(b) If the HUD-insured mortgage is prepaid in full, the holder of the residual receipts note has the right to declare the whole principal sum or any balance with interest immediately due and payable.

(c) Prepayments to principal and interest:

(i) may be made (a) from the residual receipts as defined in the Regulatory Agreement only after obtaining written approval from HUD or (b) from sources other than Project Income or Project Assets, e.g., syndication proceeds.

(ii) may be made only after final endorsement of the insured mortgage and after the end of a semiannual or annual fiscal period.

(iii) if unauthorized prepayment is accepted, the funds shall be returned to the Project immediately upon discovery.

(d) The residual receipts note is nonnegotiable and may not be sold, transferred, assigned, or pledged by the payee.

(e) Presentation, demand and notice of demand, nonpayment and protest of the residual receipts note are waived.

(f) Interest on the note must not be compounded.

(2) Form HUD-92223M, Surplus Cash Note (for all other mortgagor entities; formally called the Promissory Note). The conditions and limitations are the same as Form HUD-91710M, except that:

(a) Provisions may be made for interest payments annually or semiannually or at the end of a fiscal period. However, terms of the note should include the fact that interest accrues and is payable in full when the note matures.

(b) Prepayment of principal or any payment of interest must be limited to sources other than Project Income or Project Assets, e.g., syndication proceeds or surplus cash as defined in the Regulatory Agreement.

(c) Payments on promissory notes will be made only as permitted by the applicable Regulatory Agreement, but prepayment of the promissory notes from sources other than the project is permitted without HUD approval.

(d) Should any unauthorized prepayments be made, as determined by HUD, it shall be the responsibility of the Borrower to return them to the project.

(e) Interest on the note must not be compounded.

E. Tax Credit Equity Bridge Loans.

Tax credit equity syndicators or investors (with or without an identity of interest with the MAP Lender) may make equity bridge loans to LIHTC, Historic or New Markets Tax Credit projects during the construction or substantial rehabilitation period before the property's placed in service date. The bridge loan may be evidenced by a promissory note from the sponsor and may be secured by a pledge of the tax credits or of the limited partnership interest but may not be secured by a lien on the real estate. After the placed in service date, the bridge loan must be released and retired by the pay in of the investor's equity.

An equity bridge loan is a means of securing the sponsor's cash contribution that is required to complete construction before the LIHTCs are available to be claimed by the equity investor. The placed in service date is the date when the newly constructed or rehabilitated property has been completed and its units have been occupied by low income qualified residents. This is also when the LIHTCs are officially able to be claimed by the equity investor, and is evidenced by issuance of IRS Form 8609, Low-Income Housing Credit Allocation and Certification. The placed in service date will typically be after Final Endorsement of the mortgage. However, at Final Endorsement, all funds needed to meet the sponsor's cash contribution must be in the transaction so the sources and uses will balance and the LIHTC investors will pay in the equity to retire the

equity bridge loan at the later placed in service date.

F. Identify all subordinate loan funds in Section III "Source of Funds to Meet Cash Requirements" Form HUD-92264-A.

8.10 Firm Commitment Processing with Grants/Loans

A. In General

These instructions apply to:

1. Grants and loans to the borrower entity or its principals from a federal, state or local government agency or instrumentality.
2. Grants and loans to the borrower entity or its principals from national, regional and local community service organizations (nongovernmental source) or foundations.
3. LIHTC, Historic Tax Credit and New Markets Tax Credit equity syndication proceeds.

B. Application for Mortgage Insurance.

1. At the Firm Commitment processing stage, the applicant must:
   a. Identify the use of grant/loan funds on Form HUD-92013, Application for Project Mortgage Insurance.
   b. Submit: A commitment letter signed by an authorized agent of the governmental agency or instrumentality or the non-government source identifying:
      (a) Amount of grant/loan funds including all repayment terms and conditions and any regulatory restrictions that affect the operation of the property.
      (b) Intended use of the grant/loan funds.
      (c) Any conditions to the grant/loan and any reasons the commitment letter could be withdrawn.
      (d) That the grant/loan is not subject to a future appropriation or funding availability that it is currently in the hands of and available for disbursement by the governmental agency or instrumentality or the non-government source.
2. Any type of grant/loan not disclosed by the borrower may result in a rejected application or the issued Firm Commitment made null and void.

C. Grants/Loans from governmental agency or instrumentality.

1. Firm Commitment. HUD will review the proposed grant/loan structure, terms and conditions and the draft grant/loan documents during Firm Commitment processing or earlier, as needed. HUD will consider waivers with reasonable terms in order to facilitate coordination between FHA requirements and those of the governmental agencies.
2. Initial Endorsement
   a. Before scheduling the closing, the Field Counsel must review the grant/loan documents to assure their legal sufficiency.

b. The MAP Lender must consent in writing to the existence of the subordinate mortgage and agree that its existence does not constitute a basis for default on the first mortgage.

c. The governmental secondary financing Lender must agree to and enter into a HUD proscribed form of Subordination Agreement.

d. The borrower may use, instead of that portion of the front money escrow provided by the grant/loan, either:

(1) An unconditional irrevocable letter of credit issued by a banking institution with a rating acceptable to HUD and for a term acceptable to HUD, or

(2) An agreement entered into by HUD, the governmental agency or instrumentality, the MAP Lender and the borrower, which provides the following:

(a) HUD has:

(i) The right to approve construction advances after considering any reported noncompliance by the agency or instrumentality if the project is proceeding in compliance with approved plans and specifications.

(ii) A joint review and agreement between the MAP Lender, HUD and the governmental agency of construction progress schedules and allocation of draws.

(iii) Sole authority to resolve differences in the inspection process and the process of disbursing grant/loan proceeds.

(b) The MAP Lender will furnish both HUD and the governmental agency with copies of the approved interim advances Form HUD-92448, Contractor's Requisition, Form HUD-92403, Application for Insurance of Advances of Mortgage Proceeds, and supporting documentation.

(c) The governmental agency or instrumentality must process the advance from its grant or loan funding promptly and without adjustment. HUD or the MAP Lender will:

(i) Send the governmental agency a copy of the approved requisition for its records.

(ii) The governmental agency must notify HUD and the Lender of a need to make an adjustment the following month.

(d) The governmental agency assumes the risk for any grant/loan funds disbursed in excess of the amount approved by HUD or the Lender and agrees to replenish the excess funds within 10 working days of notification by HUD or the Lender.

(e) If a default occurs before completion of construction, the governmental agency must disburse the remaining grant/loan funds so long as the request for funds remains in the same ratio as previously authorized.

(f) The governmental agency's attorney must render an opinion that the agreement and grant/loan commitment is legally binding on present and all future administrations.

e. Grant/loan proceeds must be advanced either:

(1) Before the insured mortgage proceeds, or

(2) Concurrently and on a pro rata basis with the disbursement of the insured mortgage proceeds.

NOTE: If the grant/loan proceeds are not available at initial endorsement, HUD may either:

(a) Proceed to initial endorsement, but not disburse any insured mortgage proceeds until the grant/loan is in place and the funds are available for disbursement, or

(b) Have the borrower/sponsor fund an escrow equal to the grant/loan. Advances from this escrow must follow outstanding instructions for the disbursement of the grant/loan.

(3) Release of grant/loan proceeds cannot be conditioned on the completion of specific project improvements.

3. See Appendix 12A for front money requirements and disbursement of mortgage proceeds on LIHTC projects.

D. Grants/Loans from a non-governmental source.

1. Commitment Processing.

a. The last 3 years of audited financial statements, if available, must be submitted which evidence that the providing source has the financial capacity to meet its funding commitment.

b. If audited financial statements are not available, unaudited statements, which meet the requirements of Section 8.4.C must be provided.

2. Initial Endorsement.

a. Before scheduling the closing, HUD must review the grant/loan documents to assure the legal sufficiency of the documents.

b. The grant/loan funds must be disbursed before insured mortgage proceeds.

c. Release of grant/loan proceeds cannot be conditioned on the completion of specific project improvements.

3. All work performed with the grant/loan proceeds:

a. Must be cost certified.

b. Must conform to Davis-Bacon requirements including submission of payrolls, certifications, etc., if payment of Davis-Bacon wage rates is required by the grant/loan program.

8.11 Evaluating Nonprofit Sponsors and Borrowers

A. General

Nonprofit borrower/sponsors (whether national, regional, or local) must have the experience and financial strength appropriate for the development and ownership of the proposed property. This section sets forth the criteria for making this evaluation. The nonprofit borrower/sponsor being evaluated may not have equal strength with respect to all criteria. In transactions where the

borrower/sponsor's ownership structure contains multiple entities performing differing functions, the Lender must evaluate the nonprofit and each of the other entities on their capacity to perform its particular function, e.g. ownership, property management, acquisition, development, resident services or asset management. This includes the need for prior acceptable history of successful development, ownership and management of assets similar in size and complexity as the proposed project. Therefore, only the criteria for the areas in which the nonprofit entity has direct responsibility or authority need to be applied during the evaluation process. The eligibility of prospective nonprofit sponsor/borrower must be determined before a Pre-application approval or Firm Commitment is issued. The Lender must include in the application:

1. A description of which party is paying pre-development cost.
2. Details of any proposed rent/income restrictions on the property to be developed by the non-profit.
3. Forms HUD-3434, Certificate of Relationships and Nonprofit Motives and HUD-3435, Certificate of Contractual Relationships.
4. Developer's Agreement or any other document which shows the relationship and work responsibilities of all parties associated with the transaction.
5. Housing Consultant's contract, if applicable.
6. Memorandum of findings and recommendations.
   a. This document must include a description of the relationship between the nonprofit and any profit motivated entities involved in the transaction.
   b. The determination of eligibility or ineligibility of the nonprofit sponsor/borrower must be approved by the Hub/PC.
9. Explain in writing any nonperforming assets in nonprofit borrower/sponsor portfolio in conjunction with the REO review.

B. Required Exhibits from Nonprofit Sponsor.

1. Form HUD-3433, Request for Preliminary Determination of Eligibility as Nonprofit Sponsor and/or Borrower, and supplemental documentation. (If the loan requested is for a refinance, only complete those portions that are applicable.) This information must be submitted at the earlier of pre-application or Firm Commitment, as appropriate. Documentation must contain, but is not limited to:
2. Detailed explanation of the motivation for sponsoring the project including a history of the organization's involvement in multifamily housing.
3. Copy of sponsor/borrower's charter and bylaws as currently amended.
4. Verification from the Internal Revenue Service of the sponsor/borrower's tax-exempt status as a 501(c)(3).
   a. Copy of any ruling denying tax exemption
   b. If a ruling is pending, explain the application's legal and factual basis and current status.
5. List of corporate officers or officers of the board of directors of the sponsoring nonprofit with decision-making authority over the subject property, including their titles or positions, addresses and individual social security numbers.

6. Resumes on all principals and staff who will actively take part in the development of the proposed project. The property manager must have a minimum of 3 years of experience in managing at least 5 properties comparable to the proposed property in scale, complexity and regulatory compliance requirements. A property manager must demonstrate adequate property management experience with properties comparable to the subject property.
7. Current financial statement (balance sheet, profit and loss statement, and supporting schedules) as well as statements for the past 3 years. If available, audited statements should be submitted.
   a. If the sponsoring group/borrower has existed less than 3 years, the financial statements must be submitted from the date the group was formed.
   b. Statements must identify restricted and unrestricted assets (liquidity) along with the related liabilities and must show no material, unmitigated contingent liabilities.
   c. An officer of the sponsoring nonprofit must sign the financial statements.
   d. All statements must contain the certification of truth and accuracy and criminal certification identified in Section 8.4.B.1.b. This certification must reference the name of the sponsor and the date of the financial statements.
8. Signed written resolution of the nonprofit's directors or trustees, acknowledging the responsibilities and obligations of sponsorship and continuing ownership, and that the subject proposal reflects the will of the membership.
9. Form HUD-92013-SUPP listing current bank and trade references for the sponsor/borrower, if formed, and their officers (President, Vice President, Secretary and Treasurer). Only the identification information and questions about bankruptcy, judgment, etc. need to be completed for the officers.
10. The information contained in Section 8.3.G.1.a, b, and c if the sponsor/borrower or any officer has a prior federal default or claim.
11. Detailed statement of arrangements made or proposed for the following (listing principals involved, their relationship with the nonprofit sponsor/borrower, the terms of the arrangements and the circumstances surrounding each):
    a. Land on which the project will be built.
    b. Project construction, including selection of general contractor, subcontractors and architect.
    c. Legal and consulting services.
    d. Project financing, including any discounts.

    NOTE: A national, State or regional organization acting as a cosponsor must submit a separate Form HUD-3433 and Supplemental documentation.

12. The nonprofit sponsor must have diverse and stable funding sources with recurring revenue and, if required, a proven record of raising sufficient funds to meet its operating needs. The Lender must identify whether the nonprofit sponsor's primary funding sources are from fees on development projects or from sources such as public funding, public contracts, grants or donations that may be subject to budget or funding constraints.

C. Mortgage Credit Review Stage.

1. Review Form HUD-3433 to see if the nonprofit sponsor/borrower is qualified to start, complete and operate a project under the insured loan programs. Determine that all of the following criteria are satisfied:
   a. The nonprofit sponsor/borrower is acting on its own behalf and is not, either knowingly or unwittingly, under the influence, control or direction of any outside party seeking to derive a profit or gain from the proposed project—such as a landowner, real estate broker, contractor, architect, attorney or consultant.
   b. The nonprofit sponsor/borrower has continuity and a serious long-term commitment to supply housing for the intended resident population.
   c. The nonprofit sponsor/borrower has:
      (1) Strong roots in the neighborhood and in the local community.
      (2) A good reputation for reliability, service and commitment to the people for whom the housing is to be built.
      (3) The board of directors demonstrates ties to the local community served by the nonprofit and includes representatives on the board from the local business community.
   d. The nonprofit sponsor/borrower must fully understand the responsibilities and obligations of developing a housing project and continuing its successful operation. This is evidenced partly by:
      (1) General knowledge of the factors that contribute to project success or failure.
      (2) Familiarity with the housing programs.
      (3) Prior successful experience developing, owning and operating a multifamily project similar to the subject.
   e. Sponsor/borrower must acknowledge, by majority resolution of its directors or trustees, the responsibilities and obligations of sponsorship to develop and manage the project. The nonprofit borrower or sponsor must not have any unresolved or recent internal control or compliance findings.
   f. Sponsor or borrower and its principals are reliable based on:
      (1) Reputation and past performance.
      (2) Success and extent of previous experience, including the type of service furnished (financial, management, etc.), in providing housing or related social services.
   g. Sponsor or borrower is providing or has arranged for the professional and management skills essential to the successful start, development, completion, and operation of the proposed project.
2. Credit investigation.
   a. As with for-profit sponsors, the Lender's Underwriter must make a determination of who are the individuals and entities with decision-making and operational authority over the project. The Underwriter will provide an in-depth written analysis on the aspects of the mortgage credit review in the Underwriter's Narrative.
   b. Order data and/or commercial credit reports on the sponsor and borrower, if formed, and residential credit reports for the officers of the borrower entity and make inquiries of bank

and trade references identified on Form HUD-92013 Supp to determine basic acceptability of credit reputation and previous experience. A credit review of individual members of nonprofit board of directors is not required unless they are also a board officer with a decision-making role over the property.

c. Check for the existence of any delinquent federal debt.

d. Check with other HUD Offices in whose jurisdiction the nonprofit has done or now does business to ascertain their past experience and performance.

e. Check that the borrower/sponsor has no unresolved issues related to payment history and check credit references.

3. Analysis of financial data.

a. Determine:

(1) Amount of cash and liquid assets available for investment in the project.

(2) Whether the nonprofit entity has used prudent judgment in its past and present business affairs.

(3) Overall financial condition of the sponsoring group, particularly whether the financial statements indicate that income will be sufficient to meet the expenses incurred by the group.

b. Financial statements of many large nonprofit organizations show various fund accounts, such as general and building fund, etc.

(1) Be aware of inter fund receivables and payables that cancel each other.

(2) Do not consider restricted-use funds in the analysis.

(3) Review the Public Records section of the credit report to eliminate assets, which were used as collateral in secured borrowing.

c. The project size and complexity should be consistent with the abilities of the sponsoring organization.

D. Submitting Form HUD-3434, Certificate of Relationships and Nonprofit Motives, and Form–3435, Certification of Contractual Relationship.

1. At the Firm Application stage and prior to initial endorsement (beginning of construction in the case of insurance upon completion), the sponsor and borrower must certify on Form HUD-3434, their relationships with parties or firms furnishing land and services.

2. Such parties or firms must certify on Form HUD-3435 their relationship with the sponsor and borrower.

3. If there is a change in the certified relationship, the sponsor, borrower and other parties must furnish additional certifications with respect to each change.

4. All relationships are subject to HUD approval.

5. For refinance transactions those sections which deal with new construction may be left blank, insert “N/A.”

E. Nonprofits may earn a developer’s fee, but not BSPRA, on a new construction or substantial rehabilitation proposal under Sections 220, 221(d)(4), 231, or 241(a).

F. Nonprofit Sponsor and a Profit-Motivated Borrower Entity.

A nonprofit sponsor may establish a profit-motivated borrower entity for the purpose of owning a tax credit project or obtaining BSPRA and distributions from surplus cash. Such a request may be approved provided:

1. The Field Counsel determines that there is no legal impediment that would prohibit approval of the request.
2. The nonprofit agrees to be regulated by the terms and conditions of the regulatory agreement (Form HUD-92466M, Regulatory Agreement Multifamily Housing Projects) applicable to a profit-motivated entity.
3. The nonprofit is subject to the mortgage limitations applicable to a profit-motivated entity.
4. A working capital deposit is required.
5. A nonprofit developer's fee is not included in the mortgage.
6. If the nonprofit provides evidence that it has obtained exemption from real estate taxes, the tax exemption must run with the real estate and not with the type of sponsorship.
7. The potential tax consequences, as well as the possible effect on the nonprofit's Section 501(c)(3) status with the IRS, is determined to be acceptable.
8. Form HUD-3433 is not required for such cases.

8.12 Insurance Upon Completion

Insurance Upon Completion (IUC) is an option for new construction and substantial rehabilitation projects financed under Sections 207/223(f), 220, 221(d), and 231. Mortgage insurance is provided after project completion and issuance of Certificates of Occupancy for all units. The following instructions apply to IUC projects:

A. A financial and credit investigation will be required on the borrower and its principals.

B. MIP is not included in Form HUD-92264 nor is it charged until the project reaches endorsement

C. Working Capital and Operating Deficit Escrows. Projects that apply under IUC must meet the operating deficit escrow and working capital requirements as outlined below, except for the extra 2% construction contingency portion of the working capital requirement.

D. Assurance of Completion is not applicable to IUC projects. At endorsement, the general contractor must address latent defects by:

1. Entering into the latent defects agreement with HUD
2. Funding a cash escrow deposit equal to 2.5% of the mortgage, or
3. An irrevocable, unconditional letter of credit issued to Lender by a banking institution, or
4. The Latent Defects Escrow, HUD-92414M, requires a latent defects escrow of 2 ½% of the total amount of the Construction Contract, in the form of a surety bond, cash escrow or letter of credit.

E. Breakdown of Financing Charges: In IUC projects, before issuance of the Firm Commitment,
   1. The mortgagee must provide:
      a. A breakdown of financing charges and discounts by submitting Form HUD-92455M, Request for Endorsement of Credit Instrument, Certificate of Mortgagee, Borrower and General Contractor, with the Certificate of Mortgagee portion completed. The balance of the Form is to be completed before Final Endorsement in lieu of Form HUD-92023M.
      b. Information relative to the construction and permanent interest rates and mortgage term.
   2. Each item is reviewed to ensure its reasonableness in relation to comparable projects and market conditions
   3. HUD will inform the borrower of the fees that are recognizable for cost certification.

F. Building Loan Agreement, Form HUD-92441M, is not applicable to IUC projects.

8.13 Determining the Estimated Cash Requirements for Completing the Project

The MAP Lender must evaluate the Borrower's and its principals' financial strength and creditworthiness, including their ability to meet the financial requirements for completing a project. The Lender's underwriter is responsible for completing the Form HUD-92264-A and presenting their analysis of the cash requirement to close the transaction. To calculate the financial requirements, the Lender must total the following:

A. Total estimated development cost, including the amount by which the:
   1. Contractor's and/or borrower's estimate for construction exceeds Lender's estimate;
   2. Owner/Architect Agreement for design and/or supervisory services exceeds Lender's estimate; or
   3. Consultant's contract for services exceeds Lenders estimate.

B. Amount necessary to clear all debts on the land (or property if substantial rehabilitation). The Lender must verify all indebtedness that must be paid off at endorsement. In purchase transactions, include other costs associated with the acquisition that will not be recoverable form mortgage proceeds, such as zoning expenses.

C. Estimated cost of offsite improvements and demolition.

D. Cost of equipping and furnishing a project with non-realty items, if applicable. Use the higher of Lender's estimate or the borrower's estimate.

E. Working capital deposit, if required.
   1. The working capital escrow requirement for new construction transactions will be 4% of the mortgage amount, half of which will be a construction contingency for cost overruns and approved change orders. Separate provisions within the working capital escrow will govern the 2% construction contingency. The construction contingency portion of the escrow will be

refunded to the developer at Final Endorsement if not used. Construction funded from the contingency portion of the working capital escrow will not be considered as the basis for a request for an increased mortgage amount.

2. Working capital funds are not mortgageable and the unused portion will be returned to the Borrower if not needed. See Chapter 12 Section 12.15 for release of escrow.

3. For LIHTC projects with a funded working capital reserve held by the partnership (even though controlled by the syndicator or investor and not by HUD or the Lender), the funded reserve will be credited towards the increased construction reserve requirement, although the Lender controlled account must still meet the 2% working capital escrow requirement.

4. The working capital escrow requirement for substantial rehabilitation projects is 2% of the mortgage amount.

5. Use Form HUD-92412-M, Escrow Agreement for Working Capital. The Lender will deposit said funds in an account insured or guaranteed by a federal agency. See Handbooks 4350.4, Insured Multifamily Mortgagee Servicing and Hub/PC for the depository requirements.

F. Operating deficit escrow.

1. For market rate or affordable new construction, and for substantial rehabilitation projects in which there will be significant resident displacement resulting in negative cash flow during the rehabilitation period, the operating deficit escrow will be the <u>greater of</u>:

   a. What the appraisal and underwriting analysis determines to be appropriate, or

   b. 3% of the mortgage amount, or

   c. 4 months debt service (Principal & Interest and Mortgage Insurance Premium) if the property is a garden apartment, or 6 months debt service (Principal & Interest and Mortgage Insurance Premium) if the property is an elevator building where a single Certificate of Occupancy will be issued before any of the units or any of the entire floors can be rented.

2. HUD will consider Lender requests for operating deficit escrow draws during lease-up based on the adequacy of the remaining amount of operating deficit escrow on deposit with the project. See Chapter 12 Section 12.15.E for further mitigation and release guidance.

3. The amount of the operating deficit escrow for substantial rehabilitation projects with at least 90% project based rental assistance is only what the appraisal and underwriting analysis determines to be appropriate and need not be the higher of 3% of the mortgage amount or 4 months of debt service. The underwriting presentation should provide a detailed estimate of the projected cash flow through the period of the rehabilitation to support the lower escrow amount.

4. For LIHTC projects with a funded operating deficit reserve held by the partnership (even if controlled by the investor and not by HUD or the Lender), the funded reserve will be credited

towards the increased reserve requirements of 3% of the mortgage amount or 4 months of debt service, although the Lender controlled account must still meet what the appraisal and underwriting analysis determines to be an appropriate operating deficit amount.

5. Use Form HUD-92489a-M, Escrow Agreement for Operating Deficit. The Lender will deposit said funds in an account insured or guaranteed by a federal agency. See Handbook 4350.4, Insured Multifamily Mortgagee Servicing and Hub/PC for the depository requirements.

G. Commitment, marketing fees, and discounts must be paid out-of-pocket by the sponsor/borrower and may not be paid from the operating deficit escrow.

H. For tax-exempt or taxable bond financing, cost of issuance must be paid out-of-pocket by the sponsor/borrower and may not be paid from the operating deficit escrow.

I. Relocation payments not included in Lender's estimated replacement cost on Form HUD-92264-A may be paid from the operating deficit escrow.

From this total, the Lender must deduct the maximum insurable mortgage, any grant/ loan funds or tax credit equity attributable to replacement cost items and fees not to be paid in cash. The remainder is the estimated financial requirements needed to complete the project. These calculations should be recorded on Form HUD-92264-A.

J. Cash-Out From Land Equity.

If land, or the "as is" property value for a substantial rehabilitation project, is contributed to meet the sponsor's equity requirement, any cash out from the excess land or property equity **above** what is required at initial endorsement must be deferred (See Appendix 12A paragraph E) until the project is complete and it has demonstrated to the Hub/PC's satisfaction that it has achieved 6 consecutive months of break-even occupancy. This does not prevent applying land value equity to fund operating deficit or working capital escrows, or other cash requirements at initial endorsement. To the extent that there are excess mortgage proceeds available from land value (or "as is value") or other equity, excess mortgage proceeds may be set up at Initial Endorsement and used for all the purposes described in Appendix 12A, paragraph D, including funding the working capital construction contingency escrow. See Chapter 12 Section 12.8 and 12.15 for guidance.

K. Cash-Out / Equity from Loan Proceeds – Section 223(f).

50% of any cash out proceeds after funding any transaction costs including the assurance of completion requirements, must be held in escrow by the Lender until the non-critical repairs are completed and HUD approves the release. Critical repairs must be completed before initial/final closing. The escrow is established at Initial/Final Endorsement, on Form HUD-92476.1M, Escrow Agreement for Non-Critical, Deferred Repairs.

L. Tax Credit Equity Contribution

1. Pursuant to the Housing and Economic Recovery Act (HERA) of 2008, HUD may no longer require that a borrower place in escrow 100% of low income housing tax credit syndication

proceeds/equity (Regulation 24 CFR 200.54 added to this provision Historic Tax Credit syndication proceeds, and New Markets tax credit proceeds.) HUD will require, however, that an appropriate amount of the equity be invested in the project and applied to HUD approved items at the time of Initial Endorsement. The amount deemed by HUD to be sufficient for such purposes will depend on the circumstances of each transaction, but should be an amount that assures an ongoing relationship between the borrower and the tax credit syndicator or investor.

It is recommended that the initial installment of equity be an amount that is equal to or exceeds 20% of the total equity that will be available for the project. If less than 20% is proposed, the Hub/PC must submit a recommendation to HQ for review and approval. The Hub/PC must review the justification submitted by the MAP Lender in the Narrative Summary as to how the lesser amount is appropriate as an initial investment of equity. The Hub/PC will forward a recommendation to HQ along with supporting documentation for approval of the lesser amount. An example of Form HUD-92264-A to assist with the calculation of the amount of the initial and subsequent infusions of tax credit equity follows.

2. The initial installment of equity must be expended on the initial requisition at Initial Endorsement.

3. Example for Form HUD-92264-A.

   There is no change in the computation to determine the cash requirements and/or front money escrow on Form HUD-92264-A. The initial installment of LIHTC equity is calculated as follows:

Form HUD-92264-A Section II. Total Requirements for Settlement – Part B

1. a. Development Cost ……		$14,381,216
1. b – c Total of lines a & b ……..		$14,381,216
2. Land Indebtedness (or cash required for acquisition) ……..		$ 625,000
3. Subtotal (lines 1c + 2) ……		$15,006,216
4. a. Mortgage Amount ……..	$10,935,000	
4. b. Home funds ……	$ 650,000	
5. Fees not to be paid in cash ……	$ 0	
6. Subtotal (lines 4a+4b+5) ……		$ 11,585,000
7. Cash investment required (line 3 minus line 6) ……		$ 3,421,216
8. Initial Operating Deficit …….……....		$ 488,772
9. Other Cost (Bond cost $312,617) and $15,000 ……..…….		$ 327,617
10. Working Capital …….…..……		$ 218,700
11. Other: Social Services Escrow $55,000 + Fee $2,066,897) ……..……..……		$ 2,121,897
12. Total estimated cash requirement (sum of lines 7+8+9+10+11) ..……..		$ 6,578,202
Front money escrow, if any (subtract line 6 from line 1) ……		$ 2,796,216

Section III. Source of Funds to Meet Cash Requirements

Source A Tax Credit Equity …….. $5,027,301

Source B Developer Funds ……. $1,550,901

Total available cash for project…….. $6,578,202

The initial 20% calculation of the tax credit equity (which *should be the same as the tax credit equity amount reflected in Criterion 11*) for mortgeagable items is $1,005,460. This is based upon the mortgageable tax credit allocation of $5,027,301 x 20% = $1,005,460; it is not based on the total cash requirements for the project. The remaining cash requirements **not** being satisfied with LIHTC equity will be satisfied in accordance with outstanding instructions.

4. Subsequent Investment of Tax Credit Equity Proceeds

   a. The *Commitment for Insurance of Advances*, Form HUD-92432, should contain, among other special conditions, a requirement for evidence satisfactory to HUD of an agreement that binds the investor to timely and periodically pay to the borrower tax credit equity to contribute to the completion costs, in the aggregate amounts shown on Forms HUD-2880 and HUD-92013. See the special conditions in Appendix 4C or 4D.

   b. The actual amount of the initial equity investment should be reflected in the Firm Commitment as a special condition and listed as a line item on the initial requisition, HUD Form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds, for immediate disbursement.

8.14 Bond Financed Projects

A. Review of Financing Documents. A tax-exempt bond is a security issued by a governmental agency in which the interest income produced is free from federal income tax and sometimes free from state and/or local income tax. Financing documents associated with mortgage bonds or tax-exempt bonds are prepared and reviewed by the bond underwriter and the bonds are secured by a mortgage on one or more assets. In FHA insured transactions, these bonds are backed indirectly by an interest in the insured loan which is further enhanced by a GNMA Security.

   1. The sponsor must submit, with the application for commitment processing, a separate statement itemizing the estimated costs of bond issuance, issuer fees and discounts and financing fees to be paid out of pocket by the sponsor/borrower with an explanation of the necessity and reasonableness of each cost. The Lender's underwriter must check the statement for reasonableness, using the data from previously processed bond-financed projects and make adjustments where appropriate. This information is used to develop the Total Estimated Cash Requirement Form HUD-92264-A, Supplement to Project Analysis.

B. Loan Rates.

   1. The construction loan and the permanent loan rates may exceed the interest rate on the bond obligations. When this occurs, the spread will create a surplus of funds which must be held by the bond trustee. At initial closing, the bond counsel must supply HUD with a legal opinion stating that any investment income received by the mortgagee but not held for its own account must be under the control of the bond trustee and will not flow through the books and records

of the project. The bond documents will instruct the trustee to invest the funds in a federally insured interest bearing account, submit annual statements with the project financial statement, or the borrower may use the surplus of funds to cover costs associated with the bond financing transaction but not recognized in traditional HUD processing.

2. In many cases, the interest rate on the bonds will not be known during the commitment processing and it is not uncommon for the rate to change once the bonds have been sold and the bond interest rate has been established. If the mortgage rate changes, an amendment letter to the Firm Commitment should be issued reflecting the actual interest rate. If due to time constraints, HUD does not have sufficient time to reprocess a higher mortgage for the project:

   a. The Firm Commitment must contain the following condition:

      "Any interest savings resulting purely from a differential between the HUD processed interest rate and the actual final interest rate may not be construed as excess funds that may be used to offset costs in other categories at the time of cost certification. Any such savings must be applied as a mortgage reduction."

   b. An exception is that savings resulting from the early completion of construction may be used to offset cost certifiable overruns in other cost categories. Compute interest savings by:

      (1) Recalculating the interest line item on Form HUD-92264, using the actual interest rate for the scheduled construction period.

      (2) Subtracting the actual interest cost recognized at cost certification from the revised interest figure developed in (1) above.

3. HUD will allow a total financing and placement fee of 5.5% on bond financed applications. This limit applies to all multifamily Sections of the Act, except Section 223(a)(7) and is reflected in the replacement cost mortgage amount confirmed at cost certification.

C. Bonds may be sold at a premium to investors, whereby the investor pays an amount in excess of the face value of the bonds. The premium results from the bonds carrying a higher coupon rate than is generally available in the marketplace.

1. Any premium raised by a transaction is considered part of the mortgagee, bond underwriter, or issuer's profit. However, if a mortgagee gives something of value without the expectation of being repaid, HUD considers this to be a kickback. The one exception involves tax-exempt bond transactions where the issuer of the bonds may permit the borrower to receive some portion of the premium to offset the cost of issuance so that the mortgagee, bond underwriter and issuer are simply conduits for the transfer of funds.

2. If any of the premium is returned to the borrower, it will be considered excess investment income and treated as project income and used to reduce the total allowable cost of the project.

3. On bond financed projects, the premiums may be treated as project income under the following conditions:

a. The sponsor/borrower entity cannot benefit monetarily from the excess investment income.

b. The premium, if accessible to or given to the sponsor or borrower entity it controls, is considered as excess investment income.

c. Closing documents must detail the amount of the premium being given to the sponsor or the borrower entity it controls.

e. The premium may be used to pay for additional cost associated with the cost of issuance and may be applied to other recognizable cost overruns.

f. The borrower's accountant for an audited cost certification, or the borrower for an unaudited cost certification, must detail in the notes to the financial statement the amount of excess income received.

4. For nonprofit applications, excess income generated from premiums may be applied to recognizable cost overruns. Any excess income over and above that used towards recognizable cost overruns must be transferred to the reserve for replacement account.

5. On Section 223(f) applications, excess income generated from premiums must be transferred to the reserve for replacement account.

D. Itemized Statement of Costs. Attached to and reflected in the Lender's Certificate, Form HUD-92434M, is an itemized statement of the costs of issuance of the obligations, discounts and financing fees paid through the mortgagee.

1. The statement must explain why each individual item is necessary for the issuance of the obligations.

2. The Lender must review the amount of each item to ensure its reasonableness in relation to comparable projects.

3. A letter from the Hub/PC Director will inform the mortgagee that HUD will recognize for cost certification purposes the costs of issuance, discounts and financing fees in an aggregate amount not to exceed 5.5% included in the mortgage for all programs (except Section 223(a)(7)).

4. The mortgagee, bond underwriter, and issuer have the option of deferring collection of additional discounts, financing fees slow draw fees, etc., through the provision of Paragraph 20(G) of the Lender's Certificate (Form HUD-92434M).

a. The deferred collection of these items must be an obligation of a third party. Both the third party and the mortgagee bond underwriter or issuer must attest in writing that they will not look for payment from the:

(1) Borrower;

(2) Mortgaged property;

(3) Mortgage proceeds;

(4) Any reserve or deposit required by HUD and/or the mortgagee in connection with the insured mortgage transaction; or

(5) Rents or other income from the mortgaged property.

b. The borrower entity may issue, as evidence of the debt, surplus cash or residual receipts note to the third party for costs identified in this paragraph which HUD determines to be reasonable.

E. State and Local Bond Financed Projects.

1. Prepayment of Note. See special rules for State and local bond financed projects pertaining to prepayment restrictions and penalty charges in Chapter 11 Section 11.6.B.3.

2. State/Local Occupancy, Use and/or Rent Restrictions. Use or rent restrictions sought by the State or local jurisdiction for projects financed by proceeds from State/local tax-exempt obligations are often more restrictive than the minimum requirements of the Internal Revenue Code. The Hub Director may approve a State or local restriction exceeding the minimum requirements of the Internal Revenue Code, but only if the following conditions are met:

a. The Hub Director must determine that the restriction is not likely to have an adverse impact on project occupancy, marketability or long-term feasibility. This determination must be made on a project-by-project basis.

b. The restriction must not conflict with any applicable HUD mortgage insurance regulations or related administrative requirements.

c. The restriction must not appear in the Note, Mortgage, Regulatory Agreement or any other HUD/FHA loan document.

d. The restriction must be qualified to provide that it will automatically terminate in the event of foreclosure or transfer of title by deed in lieu of foreclosure. Such a termination provision must be included in every legal instrument (e.g., deed, land use restriction agreement, Security Agreement, or financing agreement) in which the restriction appears.

F. Pre-Cost Certification Conference Information. The Lender must demonstrate at the pre-cost certification conference that:

1. The net cost of negative arbitrage (i.e.: the escrow account yield vs. capitalized interest expense) may be recognized if there are offsetting savings in the mortgage.

2. Any rebate to the sponsor/borrower from the mortgagee, issuer or bond underwriter will reduce the mortgage at cost certification. The following are two samples of the most common types of rebates.

a. If mortgagee/bond underwriter contributes a portion of the initial service charge that was collected to pay discounts or other fees.

b. If mortgagee/bond underwriter refunds a portion of the construction loan interest to the borrower or sponsor.

8.15 Lender's Review and Recommendation

The Lender's underwriter's recommendation, after review of all processing materials and third party reports, is made in a separately bound report addressed to HUD included in the Underwriter's Narrative.

A. The report must detail the project's financial requirements and the credit capacity of the sponsors, borrower entity, its principals and the general contractor. The Lender's Underwriter's Narrative must detail the project's financial feasibility with an analysis of the primary risks and mitigants and the rationale for any waivers requested. The mortgage credit analysis must contain evidence of the financial feasibility and acceptability of the single asset entity, of each principal with decision making control and of investors providing funds for initial closing. Include, at a minimum, the:

   1. Name of the borrower entity.
   2. Composition of the borrower entity, include the tiers showing principals with control and providing the financing.
   3. Name of the general contractor, disclosing any relationship(s) with the borrower entity.
   4. Mortgage amount and controlling criterion.
   5. Financial requirements for closing.
   6. Sources of funds to meet cash requirements, including all sources and disclose how the money will be used.
   7. Ratio of loan proceeds to actual cost for the purpose of cost certification.
   8. The experience level of the development team relative to the proposed project.
   9. A credit and financial review of sponsor(s) borrower and principals and general contractor. This review must provide an overview of their financial strength, liquidity, experience, and creditworthiness and address positive and negative findings known by the Lender.
   10. Bonding requirements.
   11. Recommendation to accept or reject the proposed project.
   12. If accepted, any conditions to be included in the commitment. (See Chapter 11 Section 11.3)

B. Complete Form HUD-92264-A and exhibits for the type of mortgage proposed.

C. The Lender must transmit to HUD all borrower submissions and related documents.

8.16 Firm Commitment Processing - HUD Duties and Responsibilities

A. Receiving HUD Approval to Participate in HUD Programs Previous Participation Certification:

1. Principals of projects applying for mortgage insurance under HUD programs are subject to HUD approval based upon their experience and participation in previous HUD projects. APPS will allow HUD's business partners to submit their Previous Participation Certification (Form HUD-2530) request to HUD for processing via the Internet. APPS also will allow HUD staff to review and approve/disapprove 2530 submissions on-line via the HUD website.

   All participants required to apply for previous participation clearance must do so through APPS. Paper submissions are acceptable if the participants are having trouble with the APPS access. In any event, participants must complete baselines in APPS. To learn more about APPS, get registered, access the user guide and use the tutorial, please visit http://www.hud.gov/offices/hsg/mfh/apps/appsmfhm.cfm.

   HUD will review the principal's or participant's role in and status of previous projects, and the Lender's analysis of any defaults, mortgage relief, assignments, and foreclosures relating to these projects.

2. HUD will advise the mortgagee of its findings. If HUD rejects a principal, the principal's withdrawal does not necessarily result in a rejection of the application and HUD will determine if the remaining principals may successfully proceed with the project.

B. HUD will verify, through use of the Form HUD-92264-A and documents supplied by the Lender, the source(s) of funds to meet cash requirements.

Chapter 9

Environmental Review and Requirements

9.1 Introduction

This chapter outlines for the Lender and HUD staff the policies and procedures that the HUD staff must follow to meet environmental responsibilities. The Lender may submit any additional or updated environmental information prior to submission of the Firm Commitment deliverables. The Team Leader can direct the staff to complete the HUD environmental assessment prior to submission of the Firm Commitment deliverables in order to expedite the review, but should do so only where it is clear that the Lender will meet the deadline for submission of the Firm Commitment deliverables.

A. Legal Authorities, Handbooks, and Forms

1. All Federal agencies are required to comply with the National Environmental Policy Act of 1969 (42 U.S.C. 4321 et seq.) (NEPA), and the implementing procedures issued by the Council on Environmental Quality at 40 CFR Parts 1500-1508. HUD regulations implementing NEPA are contained in 24 CFR, Part 50, "Protection and Enhancement of Environmental Quality". Related Federal laws and authorities are listed in 24 CFR 50.4 and 40.3(i). HUD may not delegate its environmental responsibilities to others; it is required to prepare the environmental assessment and make the appropriate environmental finding. (See 24 CFR 50.11.)
2. HUD has issued two handbooks covering environmental issues: Handbook 1390.2, "Environmental Assessment Guide for Housing Projects", and Handbook 1390.4 "Guide to HUD Environmental Criteria and Standards contained in 24 CFR 51". Informal guidebooks issued by HUD on environmental issues are cited in this chapter. In addition, HUD offices may make the Guide, "Choosing an Environmentally Safe Site", which is used in the Section 202 and 811 programs, available to all projects.
3. HUD has established an environmental Form HUD-4128, "Environmental Assessment and Compliance Finding for Related Laws" that documents compliance with NEPA, and other environmental Federal laws, authorities, Executive Orders, and HUD standards. Form HUD-4128, with attached Sample Field Notes Checklist (SFNC) may be retrieved electronically from HUDClips. HUD staff will use the SFNC to provide information supporting the conclusions listed on Form HUD-4128. Existing apartment projects to be refinanced under Section 223(f) do not require an environmental assessment under NEPA (Part B of Form HUD-4128) except in extraordinary circumstances (see exclusion in 24 CFR 50.20(a)(5)), but they do need to comply with Part A requirements of Form HUD-4128. It is important to note

that the Environmental Site Assessment (ESA), which is performed as part of contamination analysis in Section 9.3, must be cited as source documentation in Part A, Item 23, and must be attached to the HUD-4128.

4. HUD's requirements in this chapter may exceed those of many State agencies. One reason for this is, if a mortgagor defaults on an FHA-insured project, HUD may become the project owner. Under Section 120(h) of the Comprehensive Environmental Response and Liability Act (CERCLA), Federal agencies that own properties are required to take "all remedial action necessary to protect human health and the environment" with respect to known hazardous substances upon disposition of the property. This requirement is beyond any liability releases under State or Federal law and by any due diligence requirements under CERCLA.

B. State, Local or Tribal Laws

1. In cases where state or local laws, tribal laws, ordinances, codes or regulations are more restrictive than Federal requirements, the applicant must comply with the stricter local or state standard unless Federal law states otherwise. An Application for Firm Commitment does not relieve an owner of responsibility for compliance with state or local requirements.
2. HUD will not assume any responsibility with respect to inspection, enforcement, interpretation or determination of compliance with such state or local requirements.
3. Where the project is located on a Native American reservation, the tribal authority may have the responsibilities of the state or local environmental protection agencies. In the Contamination Analysis, the acronym LSTF refers to "local, state, tribal or federal".
4. This chapter is not a substitute for requirements in the state or local laws, regulations, and Executive Orders regarding environmental analysis and mitigation.

9.2 Procedures

A. Lender's Responsibilities

1. All projects (new construction, substantial rehabilitation, refinancing or purchase) submitted under MAP require various submissions related to Contamination as stated in detail Section 9.3.

2. The Lender must also provide an Environmental Report to HUD as discussed in Section 9.5, which will identify any significant environmental issues to be resolved, and will help HUD staff in the preparation of Form HUD-4128 and SFNC. The Lender should not fill out Form HUD-4128 and should not fill out the SFNC. However, the Lender should use the criteria included in the SFNC and in Section 9.5 as a format for the information to be provided in the Environmental Report.

3. HUD environmental policy requires that there be a limitation of certain activities or actions by any direct or indirect parties to the transaction from the time of pre-application submission or the time of application submission (for lenders that do not submit a pre-

application package) until HUD has completed the environmental review process. Specifically, no action concerning the proposal shall be taken which would: (1) have an adverse environmental impact; (2) limit the choice of reasonable alternatives, or (3) prejudice the ultimate decision on the proposal. Certain actions do not fall within such limitations such as development of plans or designs or performance of other work necessary to support an application for Federal, State or local permits. Other actions do fall within such limitations, such as acquisition, demolition, modification of a wetland or significantly adversely affecting a historic property. If any party is unsure as to whether an action would fall within such limitations it should seek advice and possibly approval by HUD. These requirements are distinct and separate from any early start of contractually related construction activities as discussed in Chapter 13.

B. HUD Staff Responsibility

1. In accordance with 24 CFR 50.32, HUD, not the Lender, is responsible for preparing the Form HUD-4128 and SFNC and determining that there are no environmental factors that are prohibited by law, Executive Order, or regulation, or which would endanger health or safety, or would put FHA mortgage insurance or the U.S. Government at financial risk or liability.
2. HUD staff must review the Phase I ESA submitted by the Lender and must make a site visit. The site visit will help validate part of the information provided on the Phase I ESA and is useful for evaluating other environmental factors. A HUD appraiser and/or Field Office Environmental Clearance Officer (FECO) customarily make the site visit and sign-off on the Form HUD-4128 and SFNC. The Hub/PC Director, who issues the commitment, is responsible for signing Form HUD-4128.
3. Regulation 24 CFR 50.32 requires that a NEPA Environmental Assessment for a project with more than 200 apartment units be sent for review and comment to the appropriate FECO. The FECO must also be given the opportunity to review and comment on any environmental assessment in which the project is in the normally unacceptable or unacceptable noise zone. Projects such as Section 223(f) that are deemed to be categorically excluded from NEPA, but that require compliance with the Federal laws and authorities cited in 24 CFR 504, pursuant to 24 CFR 50.20(a), do not require review and comment of the FECO, but it is recommended that they be given the option when special analysis is required under such laws and authorities.
4. As part of its environmental review responsibilities, HUD may require additional environmental material from a Lender, such as a Phase II ESA, even when the Lender might not believe that such additional environmental material is necessary.
5. Environmental conditions should be identified as soon as possible in the processing, preferably at the time of the pre-application. Resolution of the issues should be reached prior to submission of an Application for Firm Commitment. These conditions will be discussed in the letter of invitation for Sections 221(d)(3) and (d)(4), 220, and 231. Any requirements that affect project design will be fully detailed. The Lender must assure that any requirements affecting project design are conveyed to the design architect for incorporation into the contract drawings and specifications.
6. HUD staff should refer to the specific directions and guidance contained in Section 9.4 for projects that involve remediation and or monitoring.

7. HUD staff shall promptly notify the Lender that it will take appropriate action to insure that the objectives and procedures of HUD environmental policy are achieved if it becomes aware that an action subject to limitation as discussed in Section 9.2A.3 has taken place or may be about to take place.

C. When to Submit Required Exhibits to Resolve Environmental Issues

1. For Lenders that use the pre-application process for new construction or substantial rehabilitation proposals, rather than going directly to Firm Commitment submission, HUD requires various submissions regarding contamination pursuant to Section 9.3 and the Environmental Report pursuant to Section 9.5 so that HUD can determine that all environmental issues can be resolved at the Firm Commitment processing stage The purpose of asking for certain documents at the pre-application stage is to help make an early evaluation of any environmental issues to be resolved. It does not mean that all the documentation required for environmental review need be submitted at the pre-application stage. Important issues should be resolved at the pre-application stage, with documentation on the issues submitted with the Application for a Firm Commitment. The letter of invitation will condition the issuance of a Firm Commitment upon a finding on the Form HUD-4128 that there are no unresolved environmental concerns.
2. For affordable projects that can go directly to Application for Firm Commitment, Lenders must submit all the exhibits necessary to resolve any environmental issues at the time the application is submitted.
3. Remediation of site contamination is discussed in Section 9.3 below. The implementation of plans which provide a remedy to environmental conditions may, with HUD approval, continue throughout the construction period. The Lender must identify any plan for the cure of any environmental problems which will not be solved by the time the Application for a Firm Commitment is submitted. HUD will review the Lender's plan and, if it is acceptable, will make the plan a condition in the Firm Commitment, including any plans for remediation of soil contamination, wetlands mitigation, noise abatement, historic preservation, and/or floodplains map revisions.
4. Removal or containment of lead-based paint or asbestos may continue beyond Initial and Final Endorsement if HUD approves.

D. Qualifications of Professionals

1. The sponsor/developer will generally select the professionals who prepare the Environmental Report, the Phase I ESA, or any other environmental information required by HUD, but the Lender should verify that the professionals used are qualified for their assigned responsibilities. The Environmental Professional preparing the Phase I ESA must meet all of the qualification requirements of Appendix X2 of ASTM E 1527-05 and must meet the license/certification, education, and experience requirements of Section X.2.1.1(2)(i), (ii), or (iii), of Appendix X2 of ASTM E 1527-05. The environmental professional must describe how she/he meets these qualifications in the Qualification(s) of Environmental Professional(s) Section of the Phase I ESA. For "relevant experience", such discussion must be specific as to how the requirements of SectionX.2.2 of Appendix X2 of ASTM E 1527-05 have been met. The Phase I ESA must clearly indicate that HUD is an authorized user of the

report. An example of an insufficient discussion of relevant experience would be stating that he/she performed sample analyses in a laboratory along with writing associated reports, unless such discussion indicated an "understanding of surface and subsurface conditions" and the "develop[ment of] opinions regarding conditions indicative of a release or threatened release."

2. For a Phase II ESA the "Phase II Assessor" must meet all of the qualification requirements of Section 3.1.33 of ASTM E 1903-11.
3. Other professionals may be required to evaluate technical areas, such as flooding or soil stability conditions. The Lender should assure itself that these technicians are qualified and, when these professionals are required, the Lender may contract for the services, if the sponsor/developer has not done so.

E. Consulting with the Hub or Program Center

Lenders should consult early with Hub/PC staff on HUD environmental requirements. Local conditions and interagency relations affecting environmental review requirements differ from State to State and from field office to field office. For instance, coastal zone management requirements are not applicable in most states, but in states where they are applicable, compliance procedures differ. In some states, a letter from the state coastal zone management agency for projects in the coastal zone is required but in others, alternative review procedures make this unnecessary.

9.3 Contamination Analysis: Phase I and Phase II Environmental Site Assessments and Remediation

The purpose of this section is to identify any manmade contamination on a site, other than contamination from in-place building components such as asbestos containing materials (but see Section 9.5.B) or lead-based paint (but see Section 9.5.A) and to ensure that any contamination so identified is mitigated to the point where it would be unlikely to "affect the health and safety of occupants or conflict with the intended utilization of the property" as stated in HUD-wide policy at 24 CFR 50.3(i)(1).

A. Phase I Environmental Site Assessment (ESA)

1. Submission. The Lender must submit a complete Phase I ESA with the pre-application or, if the pre-application stage is omitted, with the application for Firm Commitment. A summary submission is not acceptable. The Lender must inform the ESA preparer of all of the following Phase I ESA requirements:

   a. Purpose. The Phase I ESA will make an initial determination as to the presence of "hazardous substances" as defined by CERCLA, and of petroleum and petroleum products. However, HUD requires an initial determination not for CERCLA purposes, but rather as a part of the Department's overall environmental responsibilities pursuant to 24 CFR 50.3(i).. This purpose must be described in the "Purpose" subsection to the required "Introduction" Section of the Phase I ESA.

b. Format. The Phase I ESA must be prepared in accordance with the requirements of ASTM E-1527-05 "Standard Practice for Environmental Site Assessments, Phase I Environmental Site Assessment Process." using the table of contents and report format specified in Appendix X4, thereto.

c. Timing. The Phase I ESA must be conducted (meaning the earliest of the date of the site visit, records review documents, or interviews) within one-year of the submission to HUD. A Phase I ESA that was conducted more than 180 days prior to the submission date to HUD, but within the allowable one-year period, must be updated pursuant to Section 4.6 of ASTM E 1527-05. A Phase I ESA prepared more than one year prior to submission to HUD, even if updated within 180 days of being submitted, is not acceptable.

d. Preparer's Qualifications. The Qualifications of the environmental professionals section of the Phase I ESA must describe the preparer's qualifications.

e. Findings Section. The Findings section of the Phase I ESA must list obvious Recognized Environmental Conditions (REC), suspected or potential RECs as determined from statements made in earlier sections in the Phase I ESA, Historical Recognized Environmental Conditions (HREC) and de minimis conditions (such as minor soil staining).

f. Opinions Section. The Opinions Section pursuant to Section 12.6 of ASTM E 1527-05 must discuss each finding from Findings Section and whether it is a REC. The justification for any finding deemed not to be a REC must be included in the Opinions section. If the ESA preparer cannot make a statement as to whether a condition is or is not a REC, the Opinion Section must state what information or further investigation – such as gaining access to a building a so called "data gap," but not including a Phase II ESA -- would be deemed necessary to make such a determination. When previous remediation has been performed or is ongoing - i.e., not yet an HREC at the proposed site, the Phase I ESA must fully discuss the extent of such remediation in this section of the Phase I ESA, including any involvement of LSTF Authorities. The Phase I preparer must justify whether such ongoing remediation should resolve any RECs or undecided issues identified in the ESA. Warning: Even if the Environmental Professional preparing the Phase I ESA, determines that a Finding made in Section C.1 does not rise to the level of a REC, HUD may nevertheless determine that indeed, there is a REC.

   Note: Even if the preparer determines that a Finding made in Section C.1 does not rise to the level of a REC, HUD may independently determine that there is a REC.

g. Conclusions Section. The Conclusions Section pursuant to Section 12.8 of ASTM E 1527-05 regarding a determination of a REC must include one of the two quoted statements therein.

h. User Provided Information Section. The applicant, or the current property owner (if different from the applicant), shall complete the User Questionnaire(s) as per Appendix X3 of ASTM E-1527-05 which must be included in the "User Provided Information Section" of the Phase I ESA and the preparer must take into account any information provided in the preparation of the Phase I ESA.

i. Testing Not Required. The Phase I ESA does not require **sampling and** testing which will be performed during the course of a Phase II ESA or as part of a remediation plan (see below). However it may reference and discuss a prior Phase II ESA performed in general accordance with ASTM E1903-11 including whether a condition is a REC.

j. Vapor Encroachment Screen. The Phase I ESA must include an initial vapor (a.k.a. gas) encroachment screen to determine if there is a potential for vapors to occur in the subsurface below existing and/or proposed on-site structures. Those hazardous substances may be petroleum and petroleum products that consist of volatile organic compounds (VOC), semi-volatile organic compounds (SVOC) and inorganic volatile compounds. The initial vapor encroachment screen amendment to the Phase I ESA shall be performed using Tier 1 "non-invasive" screening pursuant to ASTM E 2600 - 10 "Standard Guide for Vapor Encroachment Screening on Property Involved in Real Estate Transactions, Section 8". If the Tier 1 vapor encroachment screen determines that, as indicated in ASTM E 2600-10, Section 8.7.1, there is a "vapor encroachment condition" (VEC) which is the "presence or likely presence" of such vapors in the subsurface below existing and/or proposed on-site structures, a likely VEC, or that a VEC "cannot be ruled out", it must be deemed to be a REC for purposes of the Phase I ESA.

k. Lead-based Paint (LBP) Chips. LBP chips that are not inside or part of a structure may be deemed to be a hazardous substance under CERCLA (see EPA document referenced at Section 9.3.C.1.c.iv, below). Therefore, if there is or was a structure on the site that was built prior to 1978, any evidence of paint chips not inside or part of any current structures must be discussed in the "Site Reconnaissance" section of the Phase I ESA, must be listed in the Findings Section, and must be discussed further as to whether the paint chips are either a REC or a de minimis condition in the Opinions section.

l. Previous Remediation. When previous remediation has been performed, or remediation is currently taking place, the Phase I ESA must fully document such remediation, including any involvement from LSTF Authorities.

m. Evaluation of the ESA. The Phase I ESA will be evaluated by HUD to determine if the property is acceptable for the hazards reviewed. If it is unacceptable because it shows an identifiable hazard, i.e. a REC, as described in ASTM E 1527-05, and no corrective action is deemed feasible, HUD may reject the property.

B. Phase II ESA

1. Purpose. The purpose of the Phase II ESA is to ascertain by chemical testing of samples and within the requirements of ASTM E 1903-11, "Environmental Site Assessments: Phase II Environmental Site Assessment Process", whether the RECs identified in the Phase I ESA have resulted in the presence of "hazardous substances" as defined by CERCLA, and of petroleum and petroleum products at levels that would exceed the Statewide, non-site specific criteria (de minims levels).

2. Timing. The Phase II ESA shall be submitted at the same time as the Phase I ESA.

3. When Required. A Phase II ESA is required if:

   a. The Phase I ESA indicates that there is a REC and corrective action is potentially feasible,

   b. The Phase I ESA comes to no definite conclusion regarding the presence of a REC, or

c. HUD requires a Phase II ESA for reasons that are described to the Lender.

4. Exception to Submission Requirement. In some cases wherein it is obvious that remediation will be required, with HUD permission, a separate Phase II ESA maybe bypassed but rather incorporated within the "site characterization" segment, of the remediation plan reference in Section 9.3.C.1 below.

5. Standards to Use. The Phase II ESA is to be performed pursuant to the logic model of ASTM E 1903-11, Section 7, such as developing the conceptual model and validation.

6. Report Format. The Phase II ESA must be prepared in accordance with the requirements of ASTM E 1903-11 using the table of contents and report format specified in Appendix X3.2 as amended by X3.3. Some of the steps that a Phase II assessor might perform may be intuitive in nature, but they nevertheless must be included in the report so as to ensure its scientific validity.

7. New Construction or Substantial Rehabilitation Projects using Pre-application. For new construction or substantial rehabilitation projects with a pre-application, the Phase II ESA, if required, shall be submitted by the Lender with the pre-application and must be reviewed by HUD before an invitation letter is issued.

8. HREC. If the Phase I ESA indicates that there is a HREC, as described in ASTM E 1527-05, i.e., a hazard has been remedied and an LSTF Authority has issued a No Further Action (NFA) letter or similar approval, HUD may either deem the NFA as completion of the remediation or it may require a Phase II ESA and/or further remediation.

9. Natural and Extent of the Study. The Phase II ESA need not necessarily be a complete site characterization (total nature and distribution) of contamination, but must proceed to a point where it indicates the location of greatest concentration and risk. However, when the existence of elevated levels of contaminants is confirmed, a complete site characterization will be required as a first step in remediation per Section 9.3.C.1 below.

10. Vapor Encroachment/Vapor Intrusion. If it is determined that there is a potential for vapors to occur in the subsurface below existing and/or proposed on-site structures either identified from the Phase I ESA as a REC or from this or a prior Phase II ESA, the Phase II ESA shall include either a Tier 2 vapor encroachment screen (per ASTM E 2600-10, Section 9), a vapor intrusion assessment (VIA) pursuant to LSTF policy and/or procedure (as discussed in ASTM E 2600-10, Appendix X7.1), or go directly to a Tier 4 "mitigation" (per ASTM E 2600-10, AppendixX7.1 or 7.2).

    If a Tier 2 screen was performed and it determined that there was a VEC, a likely VEC, or that a VEC could not be ruled out, either a vapor intrusion assessment (VIA) pursuant to LSTF policy and/or procedure or Tier 4 "mitigation" (per ASTM E 2600-10, Appendix 7.1 or 7.2) is required.

    If a VIA was performed, any mitigation (or remediation) deemed necessary must follow LSTF policy and/or procedure.

11. Phase II Conclusion. The Phase II ESA must conclude that:

    a. There are "hazardous substances" as defined by CERCLA, and/or of petroleum and/or petroleum products at levels that exceed the Statewide, non-site specific criteria and list any chemicals so found, or

b. No hazardous substances, petroleum or petroleum products have been identified above de minimis levels.

12. Off-site contamination conclusion. The Phase II ESA must indicate whether there is a risk of off-site contamination migrating on to the proposed site including if:

    a. There is no known or perceived off-site contamination in the vicinity of the proposed site,

    b. It is unlikely that any known or perceived off-site contamination will migrate on to the site, or,

    c. It is likely that known or perceived off-site contamination will migrate on to the site.

13. The Phase II ESA written report must describe how it conforms to any applicable LSTF requirements and must includes a detailed, common language summary.

14. Exception of requirement for Phase II preparation and submission for ongoing remediation. A Phase II ESA is not required when remediation is ongoing to the point of not yet being an HREC (see Section 9.3.A.1.e, above), if the Phase I ESA preparer states that such remediation should resolve any RECs and undecided Phase I ESA issues, (see Section 9.3.A.1.f, above), and if the remediation plan preparer indicates that all of the Phase II ESA requirements have been met.

C. Remediation Plans - General

Remediation plans are required if the Phase II ESA cannot make the determinations required by Section 9.3 B.11.b, and B.12.a or B.12.b. The following requirements apply to all remediation plans:

1. Complete site characterization.

    a. Anytime a site has been identified from a Phase I or Phase II ESA as having contamination (or contamination exposure pathways), be it vapor (gas), liquid, solid, dissolved, or non-aqueous phase liquid (NAPL), above de minimis levels, a complete site characterization (sometimes known as special site assessment report, a detailed Phase II ESA, or a Phase III ESA) must be prepared as the initial step of any remediation plan.

    b. It must determine the total nature and distribution of such contamination, exposure pathways, and potential receptors (a.k.a., a conceptual site model). However, if the remediation plan preparer determines that the Phase II ESA preparer has already determined the total horizontal and vertical extent of such contamination, exposure pathways and potential receptors, then such determination shall be so indicated and the Phase II ESA shall be made a part of the remediation plan.

    c. It must be based on the appropriate combination of the following ASTM Practices and Guides, as amended, as determined by the remediator's environmental investigator. Lesser degrees of site assessments or non-conformance are not acceptable. For lead contaminated sites, refer to the listed EPA Handbook.

        i. D 6235-04, "Practice for Expedited Site Characterization of Vadose Zone and Groundwater Contamination at Hazardous Waste Contaminated Sites"

ii. E 1689-95 "Standard Guide for developing Conceptual site models for Contaminated Sites"

iii. E 1903-97, "Environmental Site Assessments: Phase II Environmental Site Assessment Process"

iv. E 1912-98, "Guide for Accelerated Site Characterization for Confirmed or Suspected Petroleum Releases"

v. EPA, Superfund Lead-Contaminated Residential Sites Handbook, 2003

d. The requirements of Section 9.3.C.2, 3, and 4 must be met.

e. It must discuss how it complies with the listed Practices or Guides and/or the appropriate LSTF procedures.

f. It must indicate how it meets the requirements of any applicable LSTF regulatory procedures.

2. Any remediation studies and plans must be in the form of a report which includes a detailed, common language summary and discusses how it meets the listed Practices or Guides and/or the appropriate LSTF procedures.

3. Any remediation studies and plans must be presented to HUD at the same time as the Phase I ESA and, if applicable, the Phase II ESA.

4. The remediation plan preparer's qualifications must be discussed in any remediation reports.

5. For Lenders using the pre-application process, the remediation plan must be submitted at the pre-application stage, and must be reviewed by HUD before an invitation letter is issued. Evidence of approval of the remediation plan by the LSTF authority must be submitted with the Application for Firm Commitment.

6. The remediation plan must cover all relevant contaminant phases: vapor (gas), liquid, solid, dissolved, and NAPL.

7. If HUD determines that it is uncertain whether implementation of the remediation plan will remove the contamination or bring it to a de minimis level, the remedial work must be completed, including clearance testing, and the remediation itself must be approved, including issuance of any clearance and closure documents, by the LSTF authority prior to issuance of the Firm Commitment.

8. If the extent and cost of removing the contamination can be definitively determined, and the cost of removing that contamination can be specified pursuant to a contract for remediation (see Section 9.4), HUD may allow a remediation plan that has been approved by the LSTF authority that:

   a. Permits the remediation including site testing, any clearance and closure documents, and the approval by the LSTF, prior to Initial Endorsement, or

   b. If the applicant can show why it would be impractical to complete remediation prior to Initial Endorsement, permit the remediation including site testing, any clearance and closure documents, and the approval by the LSTF, prior to Final Endorsement and initial occupancy. (See Section 9.4 for remediation costing.)

9. All residents living regularly and construction workers working regularly on site while remediation is taking place shall be informed of the remediation activities and protected from any potential contamination. This requirement must be a part of the remediation plan.
10. Remediation contract insurance. Unless HUD determines otherwise, the remediation contract shall require cost cap and reopener insurance coverages, copies of which are to be included in the remediation plan.
11. Ongoing Remediation. If remediation is taking place or has been completed but has yet to receive approval by the LSTF at the time of submission of the Phase I ESA, the remediation plan and all remediation studies shall be submitted, along with a detailed common language summary, at the same time as the Phase I ESA.

D. Remediation Plans – Complete Removal of Contamination

1. Except for situations where Section 9.3.E (Remediation Plans Allowing for Incomplete Removal of Site Contamination) applies, the Lender must submit a remediation plan designed to bring the contamination identified by a complete site characterization per Section 9.3.C.1 to de minimis levels or eliminated to the extent necessary to meet the LSTF authority standards, with no ongoing active or passive remediation. There must not be any need for engineering controls, institutional controls, or monitoring wells.
2. All of the requirements for Section 9.3.C must be met.
3. A remediation plan that involves control of off-site contamination per Section 9.3.G and/or Tier 4 vapor encroachment mitigation per Section 9.3.B.10 is not permitted under this section but may be allowed under Section 9.3.E.

E. Remediation Plans – Incomplete Removal of Contamination

1. If the costs are deemed to be exorbitant and/or the feasibility deemed impractical for remediation of on-site contamination to de minimis levels, or if there is known or expected offsite contamination that poses a risk to the project site, the remediation plan may allow for incomplete removal, as described below. Justification for such incomplete removal must be submitted along with the remediation plan and must include documentation that shows that the cost of the incomplete removal of contamination, including any life cycle costs for Operation and Maintenance and any applicable enforcement requirements of LSTF authorities, are sufficiently below the costs of complete contamination removal, per Section 9.3.D above.
2. All of the requirements for Section 9.3.C must be met.
3. The corrective action must be a Risk Based Corrective Action (RBCA) based on the appropriate combination of:
   a. The following ASTM Guides and Practices, as determined by the remediator's environmental investigator (for lead contaminated sites, refer to the listed EPA Handbook):
      i. E 1689-95 "Standard Guide for developing Conceptual site models for Contaminated Sites"
      ii. E 1739 – 95, "Standard Guide for Risk-Based Corrective Action Applied at Petroleum Release Sites"

iii. E 1943 – 98, "Standard Guide for Remediation of Groundwater by Natural Attenuation at Petroleum Release Sites"

iv. E 2081 – 00, "Standard Guide for Risk-Based Corrective Action"

v. E 2091 – -05, "Standard Guide for Use of Activity and Use Limitations, Including Institutional and Engineering Controls"

vi. E 2435 – -05, Standard Guide for Application of Engineering Controls to Facilitate Use or Redevelopment of Chemical-Affected Properties"

vii. WK16004—"Draft Standard Guide for Risk-Based Remedy Selection" (when issued)

viii. E 2600 - 10 "Standard Guide for Vapor Encroachment Screening on Property Involved in Real Estate Transactions."

ix. For Lead Contaminated Sites. "EPA, Superfund Lead-Contaminated Residential Sites Handbook, 2003"

b. LSTF regulatory procedures may be followed in lieu of the ASTM Guides and Practices, as listed above, when the remediator's environmental investigator determines they are equivalent to the ASTM standards or of greater stringency.

4. The RBCA must always meet the requirements of any LSTF regulatory authority.

5. The RBCA report(s) must:

   a. Meet all of the requirements of Section 9.3.C, and

   b. Discuss how the remediation plan complies with the applicable ASTM Guides and Practices and/ or LSTF regulatory procedures as discussed in Sections 9.3.E.3.b and 9.3.E.4, above.

   c. Discuss how it meets or will meet all of the requirements of Section 9.3.E.6.

   d. Discuss how it meets or will meet all of the requirements of Section 9.3.F through J.

6. The corrective action must be an RBCA supported by the applicable combination of:

   a. Engineering and Institutional Controls (EC/IC).

      i. An appropriate mix of engineering controls such as capping and slurry walls, and institutional controls such as protective covenants and access restrictions are usually required for all RBCAs, shall follow the guidance in ASTMs E 2435- 05 and E 2091-05 and must indicate how it met these Guides. LSTF regulatory provisions may be followed in lieu of these ASTM Guides, as amended when the remediator's environmental professional determines their equivalence.

      ii. Operations and Maintenance Plan (O&M) Plan. Any time there is an EC/IC there must be an O & M plan which itself is an IC. The O & M plan must be approved by the LSTF authority, and must discuss any associated enforcement required by LSTF authorities. An O&M plan must be in place for management of all contamination remaining on the site and any controls thereof. If HUD determines that the mortgagor does not have sufficient capacity to manage the O&M plan, the mortgagor must contract an appropriate servicer to do so. (See Section 9.4. for costing.)

iii. Hard/Soft Cap Engineering Control. A hard cap EC, such as concrete, generally is required if any contamination will remain on the site after Final Endorsement. Unless the applicant can justify why a lower depth to contamination would be protective of the health and safety of occupants, the depth of any remaining contamination should be greater than:

- the depth of the foundations of any existing or proposed structures including sumps,
- any existing or proposed utilities on site, or
- five feet below the surface.

In certain situations, HUD may allow for a soft cap (e.g. dirt) if other engineering controls such as an impenetrable geotextile fabric are included. Even if EC are not required for such RBCAs, IC is still required.

iv. Slurry Wall or Equivalent Engineering Control. A slurry wall or equivalent type EC may be required to prevent offsite contamination from migrating onsite or to prevent onsite contamination from migrating onsite or offsite. If the Phase I and/or Phase II ESA determines that the likely existence of off-site contamination presents a risk to the site, such a slurry wall or equivalent type EC will be required.

v. Monitored Natural Attenuation and Enhanced Passive Remediation (MNA/EPR). MNA/EPR such as by bio-augmentation where no additional active input is required and passive engineering controls such as a slurry wall may be allowed as part of the RBCA. In such cases, the LSTF authority must issue a conditional No Further Action Letter or similar approval. Monitoring wells pursuant to the above RBCAs and meeting the requirements of Section 9.3.F will be required to monitor the progress of the remediation. When MNA/EPR is part of the RBCA, the remediation may continue beyond Initial Endorsement provided that the LSTF authority has determined in writing that such undertakings would present no threat to health, safety or the environment.

vi. Vapor Encroachment/Vapor Intrusion Mitigation. If a VEC, a likely VEC or a VEC cannot be ruled out , then mitigation as discussed in ASTM E 2600-10, Section 7.2 is required, unless a VIA has been performed pursuant to LSTF policy and/or procedure and in ASTM E 2600-10, Appendix X7.1) and has determined that it is in compliance with such policy or would be in compliance after instituting mitigation. When remediation goes directly from a Tier 1 screen or a Tier 2 screen, such controls shall, where feasible, consist of a poured-on vapor barrier to be used in conjunction with active and passive venting systems.

vii. IC regarding groundwater contamination, if applicable is or will be put in place.

b. No Further Action Letter (NFA). The LSTF authority must issue an NFA, or similar approval, except that a conditional NFA may be allowed pursuant to MNA/EPR and must be issued pursuant to the time lines required by Section 9.3.E, above. Additionally, the LSTF authority must indicate that the remediation that has take place or will take place is protective of health, safety and the environment.

c. Groundwater Requirement. A site is or will be otherwise acceptable if contamination exists in the groundwater after completion of remediation, if:

i. IC regarding the groundwater is/will be put in place, along with an O&M plan, approval by the LSTF authority, and any applicable enforcement requirements of LSTF authorities. The ICs must prohibit any and all uses of the groundwater;

ii. The highest anticipated levels of groundwater based on high groundwater and/or100 year flooding events, are below the levels of any construction or potentially anticipated utility work unless it can be shown how such high groundwater levels will not modify the horizontal and vertical extent of contamination to such a degree that it could affect the health and safety of residents and workers; and

iii. Any vapors from groundwater and/or soils are shown not to present a significant risk pursuant Tier 1 vapor encroachment assessment, Tier 2 vapor encroachment assessment, VIA, or mitigation.

d. Safety of and Disclosure to Residents and Workers. Any time contamination above de minimis levels is allowed to remain on site after initial occupancy and final closing, all maintenance workers who might perform activities that could compromise the EC/IC, construction workers, and building residents, etc. are to be informed of the general type and extent of contamination and the protective measures that have been taken. It would be up to residents to inform any of their visitors/guests of these conditions.

e. Hazardous Substance Quantification. If any RBCA remediation plan identifies hazardous substances (listed in 40 CFR 302.4) that will remain on the property after Final Endorsement, such plan shall determine the quantity of such hazardous substances and whether it exceeds the levels indicated at 40 CFR 373.2(b). (This is a requirement under CERCLA that would apply to HUD at any, time that HUD might own the property or take over its management.)

F. Monitoring Wells, Flushing Wells, or Testing Wells

1. General Requirements. The presence of a testing or monitoring well on the property does not bar the property from consideration for mortgage insurance. If a monitoring well is required to confirm that contaminants have been removed to intended levels or that an MNA/EPR is working properly, EC/IC , will be required until such time as contaminants are reduced to de minimis levels and a Final NFA letter is issued.

2. Monitoring Well Protocols. Monitoring protocols must be specified in the RBCA and monitoring must proceed until contaminants have been removed to intended levels or that passive MNA/EPR is working properly.

3. Off-site Contamination – Acceptability. If a monitoring well is required to determine if existing or assumed off-site contamination has migrated or might migrate on-site, the site is generally not acceptable unless associated EC/IC are put in place pursuant to a RBCA or unless the LSTF authority provides a statement that such off-site contamination would not present a risk to the health of the project's occupants if it were to migrate on-site.

4. Flushing Wells – Unacceptable. In no case may Final Endorsement/initial occupancy take place when a flushing well is in operation or will be required.

5. Testing or Monitoring Wells Ordered by LSTF. A testing or monitoring well may also be placed on the property by order of the LSTF to test or monitor contamination on the site or from a neighboring site. If a monitoring well would be required or exists solely to monitor the general health of an aquifer used as a water supply or potential water supply, but not in relation to an existing or potential hazardous condition, this is not a bar to environmental approval. However, the Lender must notify HUD if there is any current or intended placement of a monitoring or testing well.
6. Non-operating Wells. Non-operating wells are not a bar to environmental approval, but must be capped over and closed out pursuant to the appropriate LSTF authority.

G. Off-site Contamination

If the Phase I and/or Phase II ESA determine that the existence of off-site contamination presents a risk to the site or the residents of the project and the sponsor has no control over the off-site locations of the contamination, the site is not acceptable unless such off-site contamination is subject to a RBCA meeting all of the requirements of Sections 9.3C and E.

H. Escrow

An escrow account must be set up and held by the Lender for the maintenance of any monitoring wells and engineering controls, such as caps or slurry walls.

I. Waivers

If a Hub/PC intends to waive any of the requirements in this Section 9.3 that are not regulatory in nature, the advice of the Departmental and/or Housing Environmental Officer or one of the Field Office Environmental Officers should be obtained before the waiver is granted to ensure that such waiver is in compliance with the environmental requirements of 24 CFR 50.3(i).

J. LSTF Approvals and Reviews

Any approvals by an LSTF authority must be given directly by that authority and may not be given by a third party approved by that authority to act in lieu of the authority itself. Approvals by local authorities are only acceptable when such authority is acting under delegation from the State.

K. Unacceptable Sites

A site over a former solid waste landfill/dump and/or Superfund (National Priorities List (NPL)) site generally is not acceptable for development unless the hazardous substances, petroleum, and petroleum products are completely removed, the site is delisted, or for an NPL site only, the Federal Agency with management authority over the site gives approval of the site for residential usage.

9.4 HUD Staff Responsibilities in Reviewing Cases Requiring Remediation

A. General Responsibilities

The Department assumes greater risk anytime that a Firm Commitment is issued on a contaminated site, which risk is even greater when a loan is on a site where complete removal of contamination is not possible, requiring monitoring possibly with continuous remediation techniques such as MNA/EPR. Therefore, HUD staff must exercise great care in the review process to assure that all reasonable measures are taken to mitigate HUD's exposure and that an accurate determination is made of any remediation costs that are included in the HUD-insured mortgage. Any special site assessment reports, Phase II or Phase III ESAs should be reviewed so that the extent of the contamination is fully understood. Although the Lender is responsible for assuring that environmental remediation contractors are qualified and experienced, field staff must still review references and qualifications and are strongly encouraged to consult with their environmental officer.

B. Complete Removal of Site Contamination

1. Valuation. Valuation is generally responsible for the review of all environmental documentation and for the preparation of the SFNC and the Form HUD-4128, which may be supplemented as needed to document the review and Valuation's conclusions as to the adequacy of the proposed remediation plan.

   Any estimates of value or rents should be made as if the project is unaffected by contamination and conditioned on successful removal. The appraisal must address any effect of marketability that may be present due to the prior environmental history.

2. A/E and Cost. The A/E and Cost staff are responsible for determining if the cost estimate of the remediation plan is reasonable and if the remediation and removal contractor is appropriately bonded and qualified. Cost data for remediation is not as plentiful as with more routine construction tasks. "Environmental Remediation Estimating Methods" might be helpful in some cases and is available through RS Means at http://www.rsmeans.com. In addition, the A/E and Cost staff may consult with local environmental remediation professionals about costs for similar work.

3. Mortgage Credit. Mortgage Credit shall administer escrow, performance and bond payment requirements. The amount of the escrow or bond shall be based on the estimated cost of the mitigation work from the contractor, at 150% of the estimated cost, or in an escrow established for the same amount. The cash requirements for the escrow or bond, and the Lender and Mortgage Credits procedures for administering the escrow, shall be in accordance with existing closing instructions in the FHA Multifamily Program Closing Guide. Higher escrow or bonding requirements will be necessary if the appraiser and/or the environmental officer determine that there is a greater than average risk that unforeseen problems may arise, resulting in increased cost, based on previous experience with similar work and/or research through local environmental remediation contractors about their experience in containing the cost within their stated estimate.

C. Incomplete Removal of Site Contamination

1. All disciplines should follow the guidance in Section 9.4.B regarding initial removal or mitigation costs.

2. Valuation must assure that the MAP Underwriter included on Form HUD-92264, the cost of any requirement for continuous monitoring and/or mitigation. This may be accomplished by including this cost in Section E of the HUD-92264 under "Other Maintenance" and would include fees charged by service providers who are engaged to perform monitoring. If an expense is for actual or anticipated replacement of a component such as a pump, it should be included in the Reserves for Replacement. The basis for the expense or additional replacement reserve will be obtained from a qualified engineer and/or contractor. The engineer/contractor's estimate should be sufficiently detailed and supported to allow review by the A/E & Cost staff as well as the Valuation staff.

   Any effect on project marketability, value or rents due to the need for continuous monitoring/mitigation must be quantified and discussed in the appraisal.

D. Management, Coordination and Communication

The Department assumes greater risk in cases involving environmental mitigation that will occur after Initial Endorsement especially when mortgage proceeds are used to fund the cost of remediation. Extra attention must be given to the need for frequent communication, preferably with written documentation, between disciplines that are coordinated by team leaders and Hub/PC Directors relating to levels of contamination, cost estimates and the certainty of the effectiveness of mitigation.

E. Insurance/Guarantee Requirements

Borrowers are required to obtain separate insurance for environmental hazards from an insurer acceptable to HUD if remediation work will be done on the site during the insured loan period, if the coverage is available. Environmental hazard insurance typically covers liability and cost of completion.

The environmental remediation contractor will almost always be different from the project's general contractor. Aside from the contractor qualifications, licensure and bonding that are addressed above, the remediation contractor must provide HUD a separate guarantee of completion for their work on a form prescribed by HUD.

9.5 Environmental Report

In addition to the submission requirements discussed above, the Lender must provide a narrative Environmental Report along with any available supporting documentation for the project, which report may be separate from the Phase I ESA or included within its body, but as a separate section. This report should cover the relevant topics in the SFNC and those issues that might affect the acceptability of the project including any issues of compliance with state environmental laws. The Environmental Report must be submitted at pre-application for those Lenders using the pre-application process, or at the Application for Firm Commitment stage for others.

Additionally, the following environmental issues should or must be included:

A. Lead-based Paint (not covered in the Sample Field Notes Checklist (SFNC)) (Mandatory)
B. Asbestos (not covered in the SFNC) (Mandatory)
C. Historic Preservation (Item 18 in the SFNC) (Mandatory)
D. Floodplain Management (Item 17 in the SFNC)
E. Wetlands Protection (Item 22 in the SFNC)
F. Endangered Species (Item 24a in the SFNC)
G. Noise Analysis (Item 19 in the SFNC)
H. Explosive/Flammable Hazards (Item 20 in the SFNC)
I. Coastal Barrier Resources (Item 16, SFNC)
J. Coastal Zone Management (Item 10, SFNC)
K. Sole Source Aquifers (Item 24b of the SFNC)
L. Airport Clear Zones (Item 21 of the SFNC)
M. Other Federal or State Laws (Item 24 of the SFNC)
N. Additional Hazards and Nuisances (covers pipelines, etc.) (Items 27 and 28 of the SFNC)

The issues discussed in detail below must be analyze by HUD staff during their preparation of the Form HUD-4128 and SFNC and provide guidance by which the Lender can assist HUD. These brief descriptions are not substitutes for the requirements in the statutes, regulations, Executive Orders, and handbooks. Note that Item 23 "Toxic Chemicals and Radioactive Materials" of both the SFNC and the Form HUD-4128 should be included in the Phase I ESA discussed above.

A. Lead-Based Paint

1. Lead-based paint, which may be present in buildings built prior to 1978, is not covered by Form HUD-4128 or the SFNC, but must be addressed by the sponsor's architect.
2. Lead-based paint requirements are applicable to multifamily housing constructed before 1978, except they do not apply to housing designated exclusively for the elderly or persons with disabilities, unless a child of less than 6 years of age resides or is expected to reside there, and do not apply to 0-bedroom dwelling units. If the sponsor believes that the lead-based paint requirements do not apply, it must be specifically discussed in the Environmental Report.
3. All HUD regulations on lead-based paint are found at 24 CFR Part 35, copies of which, along with guidance materials, may be downloaded from http://www.hud.gov/offices/lead/enforcement/lshr.cfm or obtained by telephoning 1-800-424-LEAD.
4. Under the regulation there are different requirements for:
   a. Residential properties constructed before 1960,
   b. Residential properties constructed after 1959 and before 1978, and
   c. Properties constructed before 1978 being converted from commercial or industrial to residential use and for properties built before 1978 undergoing major rehabilitation (defined as "rehabilitation that is estimated to cost more than 50% of the estimated replacement cost after rehabilitation").

5. Except for conversions and major rehabilitation, for pre-1960 residential properties, a risk assessment to identify lead-based paint hazards, performed in accordance with 24 CFR 35.1320(b) must be included in the environmental report. Any identified lead-based paint hazards must be treated with "interim controls" in accordance with 24 CFR 35.1330 and shall be considered to be completed when clearance is achieved in accordance with 24 CFR 35.1340. Interim controls generally should be completed prior to issuance of the Firm Commitment, but with HUD approval, may be completed prior to Final Endorsement under conditions in the Firm Commitment which require an escrow of sufficient repair or rehabilitation funds. Rather than perform a risk assessment and interim controls "standard treatment" throughout the property may be performed in accordance with 24 CFR 35.1335. If interim controls are required or standard treatment performed, the Firm Commitment shall require ongoing lead-based paint maintenance from regular building operations and maintenance activities in accordance with 24 CFR 35.1355(a) and the building owner must agree to incorporate ongoing lead-based paint maintenance operations and maintenance plans into routine building operations.

   Except for conversions and major rehabilitation, for properties constructed after 1959 and before 1978, the Firm Commitment shall require that ongoing lead-based paint maintenance be included in regular building operations and maintenance activities in accordance with 24 CFR 35.1355(a) and that the owner must agree to incorporate ongoing lead-based paint maintenance practices, as specified in the regulation, into routine building operations.

   For conversions and major rehabilitations, a "lead-based paint inspection" to identity the presence of lead-base paint performed in accordance with 24 CFR 35.1320(a), must be included in the environmental report. The Firm Commitment will require that any lead-based paint identified on the property shall undergo "abatement" in accordance with 24 CFR 35.1325 with the abatement to be completed prior to both initial occupancy and Final Endorsement. HUD will generally require that such abatement be achieved through paint removal or component replacement. However, if the sponsor can demonstrate that paint removal or component replacement is not practicable because the substrate material is architecturally significant and would be damaged by so doing, HUD may approve permanent encapsulation or enclosure and incorporation of ongoing lead-based paint maintenance into regular building operations maintenance activities. Such abatement is considered complete when clearance is achieved in accordance with 24 CFR 35.1340. Certain notice requirements also pertain to all three types of properties.

6. The cost of lead-based paint hazard controls may be included in the proposed mortgage loan with HUD approval.

7. Most rental transactions are also subject to the HUD-EPA lead-based paint disclosure rules at 24 CFR Part 35, Subpart A.

B. Asbestos

1. While many uses of asbestos are technically allowed today, several uses of asbestos have been banned starting in the early 1970s, and many commercial enterprises have stopped installing asbestos products as of the late 1970s. Some of the more common examples of asbestos containing materials include insulation, sprayed on finishes, such as ceilings, vinyl floor tile

and the adhesive to fix the tile in place, siding, and roofing. Asbestos is not covered by Form HUD-4128 or the SFNC, but for any proposed project site containing structures built before 1978, the topic must be included in the environmental report and addressed by the sponsor's architect. See Chapter 5 Section 5.15.A.3 and Appendices 5B and 5C.

2. On any building built before 1978, prior to HUD issuance of a Firm Commitment, a qualified asbestos inspector must perform a comprehensive building asbestos survey based on a thorough inspection to identify the location and condition of asbestos throughout any structures performed pursuant to the "baseline survey" requirements of ASTM E 2356-10 "Standard Practice for Comprehensive Building Asbestos Surveys." In those cases where suspect asbestos is found, it should either be assumed to be asbestos or should require confirmatory testing. If the asbestos survey indicates the presence of asbestos or the presence of asbestos is assumed, and if the Application for Firm Commitment is approved, HUD will condition the approval on an appropriate mix of asbestos abatement and an asbestos O&M Plan.

3. If there is asbestos and it is friable or damaged, HUD strongly recommends that it be removed. If asbestos is not friable or damaged, HUD strongly recommends that at a minimum, it be encapsulated which would be incorporated in the O&M plan.

4. Other than for asbestos abatement on a structure that will be completely demolished, the cost of any asbestos abatement activities may be included in the proposed mortgage loan.

5. All asbestos abatement shall be done in accordance with EPA requirements for air pollution prevention pursuant to 40 CFR, subpart M especially, 40 CFR 61.145 and OSHA requirements for Worker Protection, pursuant to 29 CFR 1926.1101, and any LSTF asbestos abatement and worker protection rules. All asbestos abatement must be performed by a qualified asbestos abatement contractor.

C. Historic Preservation (Form HUD-4128, Part A, No. 18)

1. HUD must follow the procedures implementing the National Historic Preservation Act (16 U.S.C. 470 et seq.) with regulations found at 36 CFR Part 800. All Applications for Firm Commitment, whether for new construction, rehabilitation, refinancing or conversion from non-residential to residential property, are considered "federal undertakings" which require HUD to make a determination of no effect, no adverse effect, or adverse effect upon historic properties**.** This is required regardless of whether the property is on vacant land, is a rehabilitation of an older property or is located in an historic district. An historic property means any prehistoric or historic district, site, building, structure, or object included in, or eligible for inclusion in, the National Register of Historic Places maintained by the Secretary of the Interior. Also, HUD must consider the area of potential effect (APE), which is often the site boundary, but occasionally the block on which the site is located or the immediate site environs.
2. To assist HUD in making its historic preservation determinations, the borrower or Lender should submit a letter to the appropriate State Historic Preservation Officer (SHPO) consisting of a narrative explaining the proposal and including the first page of Form HUD-92013. The

letter should include a map identifying the site location, the APE, and an opinion as to whether the proposal would have any effect on historic properties. The letter and the SHPO response, if any, must be included in the environmental report. Lenders may obtain from the HUD office the name and address of the SHPO who has the right to comment on the proposal. Note, that some SHPOs will not respond to applicants but only to Federal agencies. If this is the case, the Lender should contact the Hub or PC as soon as possible in the development process. The response from the SHPO need not be received by HUD prior to the Application for a Firm Commitment, but must be received by HUD before a commitment is issued.

Note: Some local HUD offices may have a Memorandum of Agreement (MOA) with the SHPO and the proposal may be part of a class of actions that do not require submission to the SHPO under the MOA (i.e. a rehabilitation of a structure that was built less than 50 years ago).

3. The SHPO is allowed 30 days (from the receipt of sufficient information from HUD) to reply to requests for consultation. If there is no reply within that time, and if there is no reason to anticipate an objection to the Application for Firm Commitment, HUD may make a determination of no effect, and a commitment may be issued. Where an undertaking will affect an historic property or historic district, the result of the consultation may be a design change, research and preservation, salvage, or in rare cases, rejection of the Application for Firm Commitment. Consultation for these procedures may take considerable time before a commitment can be issued.

D. Floodplain Management (Form HUD-4128, Part A, No. 17)

1. Applications for Firm Commitment are subject to regulations regarding floodplain management found at 24 CFR Part 55 which implements Executive Order 11988 (Floodplain Management). The borrower should check the relevant floodplain map from the FEMA. If any part of the site or integral offsite development is located within the 100-year floodplain (known as the special flood hazard area) according to the applicable FEMA map, should be discussed with HUD at the pre-application stage.

2. An application for mortgage insurance shall not be approved for a property located in (a) a floodway, (b) a coastal high hazard area, or (c) a FEMA identified special flood hazard area in which the community has been suspended from or does not participate in the National Flood Insurance Program. The terms “critical action,” “costal high hazard area,” “floodway,” and “functionally dependent use” are define in regulations at 24 CFR 55.2, 24 CFR 55.12 lists categories of proposed actions for which the floodplain management requirements in 24 CFR 55 are not applicable. As such, the floodway and coastal high hazard area prohibitions do not apply if only an incidental portion of the project is in the 100-year floodplain, or for critical actions, the 500-year floodplain and certain conditions are met.

3. New construction in mapped 100-year floodplains is strongly discouraged. This flood buffer zone is extended to the 500-year floodplain for proposed rehabilitation, refinancing, or new construction for facilities housing or serving mobility-impaired individuals – a critical use. Sites for new construction, which are in the 100-year floodplain according to the FEMA Flood Insurance Rate Map, Advisory Base Flood Elevation Map, Preliminary FIRM, or any of their official FEMA digitized equivalents, will not be considered for mortgage insurance unless one of the following steps will be taken:

a. A Conditional Letter of Map Amendment (CLOMA) or of Map Revision (CLOMR) has been obtained from FEMA prior to submission of the pre-application or, in the absence of a pre-application, prior to submission of the application for Firm Commitment. If the applicant has a CLOMA or CLOMR, HUD approval for a Firm Commitment will be conditioned on the borrower: (a) meeting the requirements of the CLOMA or CLOMR; (b) obtaining a Final Letter of Map Amendment (FLOMA) or MAP Revision (FLOMR) prior to Final Endorsement; and, (c) obtaining flood insurance on any building during the construction period until the FLOMA or FLOMR is issued.

b. If Section 9.5.D.3.a does not apply, HUD must determine if there may be extraordinary circumstances which lead to the conclusion that there are no practicable alternatives to the project site being in the floodplain. In order to make this determination, HUD and, if so, then it must conduct an 8-step decision making process which includes publishing two public notices and taking comments, as summarized in 24 CFR 55.20. In such instances, prior to issuing the first public notice, HUD will require detailed information about how the property will be altered and improvements designed. This information includes the elevation of the property, the elevation of the floodplain, and the location of life support systems. Except in circumstances where it would not be practicable, in order to minimize adverse impacts, the 8-step process shall require as a condition of any project approval that a CLOMA or CLOMR be issued prior to initial endorsement, a FLOMA or FLOMR be issued prior to Final Endorsement, and flood insurance be maintained on any building during the construction period until the issuance of the FLOMA or FLOMR. The 8-step process shall be completed before issuance of the Firm Commitment. HUD will develop the two notices, but the costs of publication will be borne by the borrower.

c. The 8-step process requires that all "critical actions" as defined in 24 CFR 55.2(b) (2), must comply with the requirements of 24 CFR 55.20(e).

4. Projects that are converting from a non-residential to a residential use are considered the same as "new construction" for floodplain management.

5. For purchase or refinancing actions described in 24 CFR 55.12(a)(2) or repair, rehabilitation, modernization or improvement actions described in 24 CFR 55.12(a)(3), an abbreviated process pursuant to 24 CFR 55.12(a) may be used by the Hub or PC to determine their acceptability. The Department will evaluate risks and mitigation measures in making its decision but it discourages these actions if the lowest floor and/or the life support facilities, or egress and ingress of the existing building, are more than 12 inches below the 100-year floodplain line.

6. Where a site does not appear to be located in the floodplain on official FEMA maps, but shows evidence of flooding, HUD is not precluded from qualitatively evaluating the acceptability of the site. Lenders will be required to provide extensive data to aid HUD in evaluating previously flooded or floodplain sites.

7. Any building accepted that is located within a FEMA mapped special flood hazard area is required to carry flood insurance under the National Flood Insurance Program for the term of the loan, in the amount of the least of: the development or project cost less estimated land value; the outstanding principal balance of the loan, or the maximum available coverage. At the time of Application for Firm Commitment, the Lender must submit a completed Standard

Flood Hazard Determination Form with proof that the new mortgagor has a commitment for flood insurance effective as of loan closing.

8. All new and renewal leases must contain acknowledgements signed by residents indicating that they have been advised that the property is in a floodplain and flood insurance is available for their personal property. This applies to properties within the 100-year floodplain and to critical actions within the 500-year floodplain.

E. Wetlands Protection (Form HUD-4128, Part A, No. 22)

1. Applications for Firm Commitment for new construction are subject to Executive Order (EO) 11990 "Protection of Wetlands" which prohibits the development or disturbance of wetlands and proposals impacting wetlands unless there is no practicable alternative and the proposed action includes all practicable measures to minimize harm to the wetland. Proposals impacting wetlands must be reviewed by HUD to determine compliance with HUD–wetland protection policy..
2. Wetlands are those identified on the National Wetland Inventory maintained by the U.S. Fish and Wildlife Service. Projects on land listed in the inventory will be considered only after HUD conducts an 8-step decision-making process which is the same as used for the flood plain process and includes consultation, issuing two public notices and taking public comment. Wetlands under local or state jurisdiction are subject to state or local review as appropriate. However, compliance with state or local requirements is not a substitute for the eight-step process.
3. Only in rare cases will rehabilitation, purchase and refinancing proposals be permitted to involve wetlands impacts.
4. The Lender must provide extensive data to aid HUD in evaluating wetland impacts and the Lender should consult early with the field office on any application for Firm Commitment on a site that impacts wetlands.

F. Endangered Species (Form HUD-4128, Part A, No. 24)

Under Section 7 of the Endangered Species Act, HUD must consult with the U.S. Fish and Wildlife Service or, where applicable with the National Oceanic and Atmospheric Administration, whenever a proposal may affect an endangered or threatened species or its habitat. A required consultation should be assumed for any site within the critical habitat (as defined in 50 CFR Part 226) of a listed species. In areas where impacts on endangered or threatened species are a concern, all appropriate information regarding possible impacts of the project should be provided to HUD as early as possible. Consultation under Section 7 may result in more stringent conservation measures than would otherwise be imposed. The Hub/PC will advise the Lender where information on endangered species may be obtained.

G. Noise (Form HUD-4128, Part A, No. 19)

1. HUD standards regarding the acceptability of noise impacts on residential property are found at 24 CFR Part 51 Subpart B, which standards must be met for new construction and conversion from nonresidential to residential projects. Where threshold criteria are met or exceeded, a noise analysis utilizing the methodology in HUD's Noise Guidebook (HUD- 953-

CPD) will be performed by HUD as part of HUD's NEPA environmental assessment. The Hub/PC should be consulted prior to attempting to design mitigation measures.

2. For rehabilitation and refinancing, noise exposure by itself will not result in the rejection of existing properties for insurance, but will be considered as a marketability factor. For rehabilitation projects, HUD will encourage appropriate noise attenuation measures for inclusion in the property alternation.

H. Explosive/Flammable Hazards (Form HUD-4128, Part A, No. 20)

HUD will not insure a property where structures and residents will be exposed to unacceptable risks posed by proximity to explosive or flammable hazards. This means that for new construction projects, and rehabilitation projects where unit density is increased or where there is a conversion from non-residential to residential or where a vacant building is made habitable, there must be an Acceptable Separation Distance (ASD) away from aboveground storage facilities with explosive or flammable material contents and similar industrial facilities. HUD standards regarding proximity to explosive or flammable hazards are found at 24 CFR Part 51 Subpart C. Analysis of sites near or in the vicinity of these types of facilities must be performed by HUD as part of the NEPA environmental assessment in accordance with the HUD guidebook: "Sitting of HUD Assisted Projects Near Hazardous Facilities (HUD-1060-CPD)". If a plan is agreed upon with HUD before the invitation letter, these hazards may be mitigated during the construction period, if the work can be done on the subject property. For projects to be purchased or refinanced, , HUD will qualitatively evaluate the risks associated with proximity to hazardous facilities.

I. Coastal Barriers (Form HUD-4128, Part A, No. 16)

Under the Coastal Barriers Resources Act and cited in 24 CFR 50.4(c), HUD is prohibited from insuring a project located within designated coastal barriers of the Atlantic Ocean, Gulf of Mexico, or the Great Lakes, known as coastal Barrier Resource System (CBRS) units and shown on associated Fish and Wildlife Service maps. A project located within a CBRS unit or, that includes a facility (such as a water main) to a CBRS unit, will not be eligible for application processing.

J. Coastal Zone Management (Form HUD-4128, Factor 10, Planning and Findings)

Projects located within a state's coastal management zone must be determined to be consistent with the approved state Coastal Zone Management program. In many states, HUD will require a letter from the State Coastal Zone Management Agency confirming consistency with the approved program. Mortgagees should be aware of the extent of coastal management zones in coastal states and contact the field office early when examining a proposal in a coastal zone.

K. Sole Source Aquifers (Form HUD-4128, Part A, No. 24)

Projects utilizing municipal water and sewer, and with appropriate local drainage and runoff approval, require no review for sole source aquifers. An aquifer is an underground body of water usually kept in place by rock, gravel, or sand. New construction and some rehabilitation projects located within the boundaries of the recharge area of a designated sole source aquifer must be reviewed by EPA for their effect on the sole source aquifer. HUD offices will identify the local, state or Federal agency with maps of sole source aquifers.

L. Runway Clear Zone, Runway Protection Zones, Clear Zone, or Accident Potential Zone (Form HUD-4128, Part A, No. 21)

1. HUD standards regarding the acceptability of property located in Runway Clear Zones (also known as Runway Protection Zones), Clear Zones, and Accident Potential Zones are found at 24 CFR Part 51 Subpart D. An Accident Potential Zone is an area at military airfields that is beyond the Clear Zone.
2. Construction or major rehabilitation of any property located within a Clear Zone is prohibited. Acquisition, refinance and minor rehabilitation of projects within Clear Zones are allowed with some restrictions. HUD must determine that projects located in Accident Potential Zones are generally consistent with Department of Defense land use compatibility guidelines for Accident Potential Zones.
3. HUD, as part of its environmental review for an existing property, shall advise the Lender who will advise the mortgagor purchasing the property that the property is in a Runway Clear Zone, Clear Zone, and what the implications of such a location are. The buyer must sign a statement acknowledging receipt of this information. HUD may reject applications for existing properties within a Runway Clear Zone or Clear Zone because of the possibility that the property may be acquired at that later date by the airport operator.

M. Environmental Justice (Form HUD-4128, Part E, No.24)

1. HUD will determine whether EO 12898, Federal Actions to Address Environmental Justice in Minority Populations and Low Income Populations, is applicable to the project. This EO requires that federal actions not result in disproportionately high and adverse health or environmental effects on minority or low-income populations. When a project impacts a minority or low-income population, or when siting of a project raises questions of discrimination, HUD will perform the necessary analysis before determining the acceptability of the project. A project that will receive a Low Income Housing Tax Credit is a clear example of when environmental justice concerns should be evaluated. HUD will advise the Lender of any Environmental Justice concerns including recommendations on their resolution. In most cases the preferred resolution would be to modify the project to eliminate or at least reduce the adverse effects, when feasible.

N. Other Federal or State Laws (Form HUD-4128, Part A, No. 24)

1. Applications for Firm Commitment are subject to provisions of other Federal authorities which seldom require action on the part of HUD, including the Wild and Scenic Rivers Act, Farmland Protection Policy Act, and the Clean Air Act. Certain State regulations also implement air quality requirements. HUD will advise the Lender if any actions under these or other Federal or State authorities are required.
2. HUD may require mitigation of a variety of additional nuisances and hazards on the property which would affect the health and safety of residents and the security of the collateral.

O. Commonly found or Observed Additional Nuisances and Hazards (Form HUD-4128, Part B No. 27 and 28)

1. All parts of any structure must be at least 10 feet from the outer boundary of the easement for any high pressure gas or liquid petroleum transportation pipeline (Form HUD-4128, Part B, No. 28).
2. No structure may be located within the easement of any overhead high voltage transmission line and must be located outside the engineered fall distance of any support structure for high voltage transmission lines, radio antennae, satellite towers, cellular towers, etc. This does not apply to local service electric lines and poles (Form HUD-4128, Part B, No. 28).
3. Additional HUD requirements for oil or gas wells, sour gas wells and slush pits are found in Form HUD-4128, Part B, No. 28. Oil and gas wells and associated slush pit requirements:
   a. Operating or planned drilling site: No residential structures are within 300 feet from the boundary of the drilling site.
   b. Operating well: No residential structures are within 75 feet of an operating well unless the following mitigating measures are taken:
      i. Nuisance controls maintenance,
      ii. Noise level controls caused by pumping, and
      iii. Spill controls to reduce risk of contamination.
   c. Abandoned well
      i. Confirmation by the State government that the well is safely and permanently abandoned and no residential structures are within 10 feet.
      ii. If there is no confirmation letter, no residential structures are within 300 feet of sour gas wells.
   d. Sour gas (hydrogen sulfide bi-product) wells: Separation distance must be determined by a petroleum Engineer, with concurrence by State government.
   e. Slush pits (used for drilling mud mixes for well lubrication):
      i. If on-site, hazards analysis is required to be performed pursuant to Section 9.3 above. Mitigation must include, but not necessarily be limited to removal of all drilling mud from the site and backfilling with clean compacted material.
      ii. If offsite, hazards materials analysis must be performed pursuant to Section 9.3.
4. If any part of a site is to be developed on filled ground, HUD may require that all grading be properly controlled to prevent differential earth movement, sliding, erosion, and/or other occurrences which might damage dwellings, streets or other improvements (Form HUD-4128, Part B, No. 27).
5. Hubs/PCs may adopt additional requirements to address unique local concerns, but, if any local requirement is mandated, the Hub/PC must inform the Deputy Assistant Secretary for Multifamily Housing and the HUD Headquarters Housing Environmental Clearance Officer of the requirement and its rationale.

Chapter 10

Management Analysis

10.1 Introduction

A. Management agents that operate insured multifamily properties play a key role in providing quality housing. While it is the ultimate responsibility of the project owner/mortgagor to select and oversee the management agent of an insured property, the establishment of an effective relationship among HUD, the owner, and the management agent is critical to the success of the property over the life of the mortgage. Detailed management documents must be submitted with the Firm Commitment application or at the pre-application stage if the management agent has been identified then. .

B. The Lender must review whether the proposed management agent demonstrates the qualifications, capability and experience to assure that the development will be managed in a prudent, efficient, and cost-effective manner and in accordance with all HUD requirements. Documentation submitted by the Lender in support of the choice of management agent must demonstrate that the agent:

1. Is eligible for approval and is in good standing with HUD;
2. Demonstrates effective management experience and acceptable operating procedures commensurate with the type of project;
3. Has adequate fidelity bond coverage;
4. Is in compliance with all state and local laws, regulations and requirements; and
5. Is able to positively communicate and cooperate with legitimate resident associations.

10.2 Exhibits Required for Firm Commitment

A. Exhibits

1. Active Partner Performance System (APPS) or HUD-2530. Participants are permitted to file either method for participation review. The Participant Certification page is required and the HUD-2530 or E-2530 Previous Participation Certification page may be submitted as early as the pre-application processing stage for all principals and affiliates of the management agent.
2 HUD-9832, Management Entity Profile for the Agent. This form provides detailed information regarding the organization, operation, and experience of the proposed management

agent. The management plan should provide a narrative overview and should include any pertinent leasing or management strategies that are not covered in Form HUD-9832.

3. HUD-9839 A, B, or C - Owner's/Management Agent's Certification, as appropriate. In this document, the agent and owner must certify that HUD requirements and contract obligations will be complied with, and that an acceptable Management Agreement will be executed. The agent and owner must certify that no payments have been made to the owner in return for awarding the management contract to the agent, and that no such payments will be made in the future.
4. Proposed Staffing for the Project. Information is required regarding the job-titles, duties, and salaries of all employees of the management agent who will work at the project which will be reviewed to determine if the number, salaries, and duties of the proposed staff is reasonable and adequate for the size and type of the proposed project. If there is a non-customary situation or arrangement, resulting in the need for more or less staff than usual, an explanation of this must be provided.
5. Resident Complaints Resolution Procedure. Provide a description of the procedure used by the agent to resolve resident complaints, as well as examples of how the system has been implemented.
6. Management Agreement, if Applicable. Projects with identity-of-interest management agents or independent fee management agents must execute a Management Agreement. An Agreement is recommended, but not required, for owner-managed projects or projects managed by a project administrator.
7. Marketing, Leasing, and (if applicable) Relocation Plan.
   a. All projects which require absorption of units at economic rents to achieve break-even occupancy must submit a detailed marketing and leasing plan and budget that has been reviewed and confirmed by the proposed management agent. The plan must discuss when marketing efforts will begin, when the leasing office and model units will be opened, how the leasing office will be staffed, and the project's marketing and advertising strategy. The plan must address timing of the construction progress schedule with respect to egress and ingress into the project, landscaping, and access to amenities. These items are in addition to those required by the Affirmative Fair Housing Marketing Plan.
   b. For substantial rehabilitation projects involving temporary relocation or displacement of existing residents, the plan must address details of timing, funding and management of the relocation process.
   c. The Lender's underwriter, the field office team leader and the Asset Management staff should review the marketing plan. Although not required, the Lender may retain a third party property management or leasing consultant to review such plans for large or complex deals or where the proposed property manager is not fully experienced.
8. Additional Information Required by the Field Office. It may be necessary to provide the field office with additional information so that a determination of the acceptability of the proposed management agent can be made.

10.3 Lender Review of Management Documents

As part of the Firm Commitment application package, the Lender must provide documentation to demonstrate the acceptability of the proposed management agent, with the Management Entity Profile of particular importance. The Lender must review the qualifications of the proposed agent to assess their ability to manage the project effectively and in compliance with HUD requirements, and must consider each of the following factors:

A. Past and Current Management

1. The Lender must review the proposed agent's past experience and current performance with respect to the following indicators:

   a. Experience with projects similar in size and configuration to the subject
   b. Billing practices
   c. Controlling operating expenses
   d. Vacancy rates
   e. Resident turnover
   f. Rent collection and accounts receivable
   g. Physical security
   h. Physical condition and maintenance
   i. Financial reporting
   j. Resident relations
   k. Resident income certification, record keeping and reporting if an affordable or subsidized project

2. If problems are identified with any of these indicators, the Lender must assess whether the agent has adequately improved its procedures to prevent the recurrence of such problems or whether management initiatives by the agent and owner are sufficient to correct the problems and their causes.

B. Ability to Manage Troubled Projects.

If the property has physical, financial or social problems that require special expertise or skills to manage effectively, the Lender must determine whether the agent has the necessary skills and expertise and whether the agent's proposed remedies for these problems are appropriate. Agents proposed for these projects should have prior experience successfully addressing similar issues.

C. Management Qualifications.

The proposed management agent should have at least one senior staff person who establishes the agent's policies and supervises project operations with the following qualifications:

1. A professional designation in housing management from a national organization that provides such accreditation, and
2. A minimum of 5 years experience in directing and overseeing the management of multifamily projects serving a similar resident clientele.

The Lender may accept a proposed agent without the experience requirements listed in this section if the agent is satisfactorily managing other insured or subsidized projects.

D. Past Performance with Identity-of-Interest Contractors.

If the management agent purchases goods or services from identity-of-interest companies and has previously managed insured projects, the Lender must assess the agent's past use of such companies and whether this use resulted in costs to the project that exceed the prices paid in arms–length transactions. The review should especially consider:

1. Goods and services purchased through any "pass-through" arrangements described in item 11(b) of the Management Entity Profile.
2. Evidence that the agent has compared prices and that the use of any identity-of-interest companies or pass-through arrangements has been more advantageous to the project than purchasing through arms-length transactions would have been.
3. Evidence that the management agent followed HUD contracting and hiring guidelines.

E. The Lender can utilize the following additional sources to determine the capability and expertise of the proposed management agent:

1. Management Entity Profile. The Lender can use the information listed on the form to solicit opinions from HUD offices that have worked with this agent.
2. Performance Evaluations for the proposed agent and projects which the agent has managed or is currently managing if those projects are under Flexible Subsidy contracts or Workout Agreements.
3. Monthly and Annual Financial Statements of the Project including the Independent Public Auditor (IPA) Internal Controls Questionnaire.
4. Additional documentation that the Lender may review includes:
   a. HUD/mortgagee on-site review reports;
   b. Correspondence;
   c. Resident complaint files;
   d. Previous management reviews; and
   e. Reviews from federal, state or local government agencies of the management agent's past experience with properties using affordable housing or subsidy programs, if applicable.

10.4 Review of Previous Participation

A. APPS was developed to automate the submission and review of the Previous Participation Certification Process (Form HUD-2530). APPS allows for four types of 2530 submissions for a management agent:

1. Baseline submissions
2. Property submissions
3. Organization change submissions
   a. Major Organization Change
   b. Corporate buyout
   c. Court Order/Inheritance
   d. Minor organization changes
4. Identity change submissions.

B. The type of submissions which HUD staff will review and which APPS will check for derogatory information on a management agent are:

1. Property submissions – all supervisory management participants in the management agent's organizational structure will be checked/ reviewed.
2. Major Organization Change Submissions – all principals in the management agent's organizational structure will be checked/ reviewed.
3. Corporate Buyout Submissions – the buyer of the management agent and all the principals in the buyer's organization structure will be checked/ reviewed.
4. Identity Change Submissions – the applicant will be checked/ reviewed.

C. APPS will check the following data sources for derogatory information on the management agent entities being reviewed:

1. Government-wide Suspensions and Debarments that APPS downloads from the GSA Excluded Parties List System (EPLS).
2. Participant Flags that HUD staff entered into APPS.
3. PPRS/F19 Participant Flags that HUD staff originally entered into that system and which have been converted into APPS.
4. Previous participation that the industry entered into APPS (with REAC and non-REAC physical inspection ratings).
5. REAC Physical Inspections.

6. Participant marks that HQ entered into APPPS.
7. Certifications that the industry entered into APPS.
8. Notwithstanding the issuance of the Commitment, previous participation approval of the management agent must be obtained prior to and as a condition of Initial Endorsement.
9. Firm Commitments may only be conditionally issued when the commitment processing is otherwise completed and all principals of the management agent are determined to be acceptable.

10.5 Bonding Requirements for Agents

The Lender must determine that the agent has adequate bonding to provide a basic level of protection for the multifamily project assets.

A. The management agent must certify in the Management Certification that it carries fidelity bond or employee dishonesty coverage for:
   1. All principals of the management entity, and
   2. All persons who participate directly or indirectly in the management and maintenance of the project and its assets, accounts, and records.

B. The fidelity bond or coverage must name the mortgagee and HUD as additional loss payees.

C. Coverage may be through one or more bonds, and one bond may cover more than one project, including projects whose mortgages are not insured or held by HUD. The agent's principals and supervisory and front-line staff may be covered under the same bond.

D. Each project must be bonded for at least the value of two months' gross potential income for the project. If a bond covers more than one project, this minimum must be computed using the project with the highest gross potential income.

10.6 Management Agreement Requirements

A. Applicability. Projects with identity-of-interest agents or independent fee agents must execute a Management Agreement. An Agreement is recommended, but not required, for owner-managed projects or projects managed by a project administrator.

B. Required contents. The owner and agent may negotiate their own form of agreement provided that it contains language to meet the following requirements:

1. Scope of services. All management agreements must describe the services the agent is responsible for performing and for which the management fee will be paid.
2. Required clauses. All agreements must provide that:
   a. Management fees will be computed and paid according to HUD requirements.
   b. HUD may require the owner to terminate the agreement:

      (1) Immediately if a default occurs under the Mortgage, Note, Regulatory Agreement, or Rental Assistance Contract that is attributable to the actions of the management agent;

      (2) Upon 30 days written notice, for failure to comply with the provisions of the Management Certification or for other good cause; or

      (3) When HUD takes over the property as Mortgagee in Possession.

      NOTE: The management agreement must always give the owner the ability to terminate the contract for cause, with no more than a 30 day notice period.

   c. If HUD terminates the agreement pursuant to its authority under the loan documents, the owner will promptly make arrangements for obtaining an alternative management agent that is satisfactory to HUD.
   d. HUD's rights and requirements will prevail in the event of any conflicts with the terms of the management agreement.
   e. The management agent must turn over to the owner all of the project's cash, accounts, deposits, investments, and records immediately, but in no event more than 30 days after the date the management agreement is terminated.
3. Prohibited "hold harmless" clause. Management Agreements cannot exempt the agent from liability for damages, injuries and losses.

C. Length/term of the Agreement. The length/term of the Management Agreement will be negotiated between the owner and the management agent. However, HUD will require a minimum one-year term. HUD may also impose a maximum term on the Management Agreement if the agent was approved by HUD on a conditional basis.

1. The Agreement may provide for a fixed term or an open-ended term (e.g., automatically renewable or "to remain in effect until cancelled by HUD, the owner, or the agent").
2. If the length /term of the Agreement changes before initial endorsement, the owner/agent must submit a new Management Certification.

D. Management Fee: The Agreement must include all specifics of the management agent compensation and how the management fee will be calculated, including any incentive management fees to be paid from surplus cash. HUD will review the fee for adequacy and reasonableness for a project of the size and complexity as what is proposed. The management fee must be equivalent to, and be no less than, a market rate fee that would be charged by a

replacement, third party management agent, if the replacement agent were to assume responsibility for management of the property.

10.7 Approval of Proposed Management Agent

A. The Lender will recommend approval to the Hub/PC of the proposed agent if the agent has demonstrated capacity to effectively manage the property within HUD requirements, the management agent has shown adequate fidelity bond coverage and the Previous Participation Certification is approved. In some instances, the Lender may find it necessary to recommend conditional approval if there are areas of the agent's procedures that are considered weak or that need to be changed. All conditional approvals will be discussed with the proposed agent and any agreements/conditions that are imposed will be shown both in the letter approving the agent, and in the Firm Commitment.

B. The Lender must provide a report regarding its review and recommendation which includes the following information:

   1. Name of the proposed management agent.
   2. Composition of the proposed management agent.
   3. Narrative of the agent's experience and capacity to operate the subject property, with particular emphasis on its past experience and capacity to manage affordable or subsidized properties, if applicable.
   4. Demonstration that adequate fidelity bond coverage is in effect and that the proposed management agreement meets HUD's requirements.
   5. A recommendation to approve the proposed management agent.

C. The Hub/PC may disapprove a proposed management agent based on the decision of the Review Committee to deny or withhold approval for the proposed agent's participation. The Committee may base its disapproval on the lack of the management agent's capacity to effectively manage the project within HUD requirements and to adequately meet the requirements of this Chapter. To proceed with a Firm Commitment review, the owner must then propose an alternative management agent (and supply all required documentation). The owner may appeal the decision of the Previous Participation Committee under 24 CFR, Part 200.241.

D. HUD will review the Lender's report and the management entity profile and make the final determination to accept or reject the proposed management agent.

10.8 Affirmative Fair Housing Marketing

The Affirmative Fair Housing Marketing Requirements (24 CFR 200.600, Subpart M) apply to all insured new construction and substantial rehabilitation projects of 5 or more units. Each applicant for insurance must submit an Affirmative Fair Housing Marketing Plan or Form HUD-935.2. The plan must describe an affirmative program to attract residents regardless of race, color, religion, sex, disability, familial status, sexual orientation or national origin to the housing for initial rental. The affirmative advertising program shall use majority and minority media and shall identity those groups within the eligible population that are considered least likely to apply for the housing without special outreach. The plan should include information on the applicant's nondiscriminatory hiring policy, its training program on nondiscrimination for its rental staff, and the display of the Department's Equal Housing Opportunity logo type and slogan. HUD must review and approve the Plan prior to the issuance of the Firm Commitment.

Applications under Section 223(f), while covered by the nondiscrimination provisions of the Fair Housing Act and Executive Order 11063, are exempt from the submission of a written plan. However, a Section 223(f) applicant is required to maintain records of its affirmative marketing efforts.

10.9 Management Agent Responsibility for Escrow Administration

Management Agents must cooperate with the Lender and with the HUD field office staff in administration of the Initial Operating Deficit (IOD) escrow, including any disbursements permitted and the release of any escrow balance remaining. The terms and procedures for release of the IOD are addressed in Section 12.15.E.

Management Agents must cooperate with the Lender and with the HUD field office staff in administration of the Reserve for Replacements account (per the reserve schedule and deposit requirements included in the Firm Commitment) and in the requirement to obtain a new Project Capital Needs Assessment (PCNA) every 10 years during the loan term. See Appendix 5 for more details on PCNAs.

Chapter 11

Lender Underwriting, HUD Review and Closing Matters

11.1 Lender Underwriting

A. Pre-application. Pre-application is required for market rate new construction and substantial rehabilitation proposals, but is optional for affordable housing proposals. The Lender's underwriter must determine that the submission meets the requirements of this Guide and represents an acceptable risk to the insurance fund. The pre-application submission to the field office must include a narrative summary prepared by the underwriter which provides:

1. A summary of the relevant data and quantitative analysis.
2. Strengths, weaknesses, risks and mitigants.
3. A summary of programmatic eligibility and technical factors considered.
4. A description of the proposed project and the surrounding market conditions, including demand, extent of competition, vacancy rates, market absorption and any other information that would be useful to analyze the proposal.
5. A description of the project sponsor (plus general contractor and management agent, if known), their qualifications, the identification of principals and a preliminary mortgage credit and creditworthiness review.
6. Explanations for any differences between the HUD-92013 application and the market study.
7. Details about features of the proposal (e.g., zoning, unusual site conditions, environmental) which may present potential problems.
8. A list of proposed in-house and third party reviewers of the application for Firm Commitment and their qualifications.

Further details on the required content of the Underwriter's Narrative and the materials to be included in the pre-application can be found in earlier chapters of this Guide that discuss the specific requirements of the insurance program for which the Borrower is applying.

B. Pre-application and Firm Commitment fees. No application fee is required for affordable housing pre-applications that submit for two-stage processing. Affordable housing borrowers must pay a review fee equal to 30 basis points of the requested loan amount with submission of the Firm Commitment application. Market rate borrowers must pay a review fee equal to 15 basis points of the requested loan amount with submission of the pre-application, which will be credited to the 30 basis point Firm Commitment fee. Applicants for Firm Commitment for programs with single stage processing must pay a review fee equal to 30 basis points of the requested loan amount.

C. Firm Commitment Application: The Lender's underwriter must review the in-house and third party reports and determine that the processing of the loan is in accordance with the requirements of this Guide and that the proposed loan represents an acceptable risk and is financially sound. The underwriter must document any changes made to the technical reports and must submit an updated, signed Underwriter's Narrative describing all relevant aspects of the mortgage transaction including a full discussion of the following:

1. Characteristics of the proposed mortgage that make it financially sound or an acceptable risk, with the reasons why the Lender recommends the loan.
2. Any risk factors and risk mitigants.
3. Changes in the project from the pre-application stage including changes in sponsorship, proposed development team and Lender reviewers.
4. Evaluation of the mortgage credit and financial capacity of the principals of the borrower and its ability to repay the loan.
5. Evaluation of the financial and technical capacity of the general contractor to build/rehabilitate the project.
6. Property financial analysis (both actual operating history and projected trends).
7. Property physical description.
8. History of borrower's equity investment in the property.
9. Analysis of market, rents, expenses and estimated rent-up and operating deficit.
10. Adequacy of the proposed Reserve for Replacement.
11. Documentation of any changes the underwriter made to the appraisal/technical reports with justification.
12. Requests for any waivers of Guide requirements with supporting documentation.
13. Certifications from the individual reviewers (see Section 11.2M).

Further details on the required content of the Underwriter's Narrative and the materials to be included in the Firm Commitment application can be found in earlier chapters of this Guide that discuss the specific requirements of the insurance program for which the Borrower is applying.

D. For applications submitted under any of the insurance programs, the underwriter who prepares and signs the Underwriter's Narrative must visit the property and examine the market conditions first hand, which cannot be delegated to others. For applications for substantial rehabilitation or refinancing, the underwriter, or an underwriter trainee acting under the direction of the underwriter, must perform an on-site lease audit and physical inspection representing a sample of each unit type. The underwriter or trainee who conducts the inspection must be identified in the narrative. Typically, the leases that are audited will be the same as the units that are inspected, as follows:

1. For projects 50 units or less: Inspect at least 1 of each unit type, to include a representative sample of 10% of the units.
2. For projects between 51 and 250 units: Inspect at least 1 of each unit type, to include a representative sample of 10 units plus 5% of the total number of units greater than 50.

3. For projects greater than 250 units: Inspect at least 1 of each unit type, to include a representative sample of 15 units, plus 2% of the total number of units greater than 250, for a maximum of 50 units.
4. The terms of the leases must be compared to the rent roll, verifying the unit number, resident name, lease commencement date, expiration date, concessions, if any, and monthly rent, and must confirm that this data is consistent with the assumptions used in the underwriting analysis.
5. Any inconsistencies or conflicts between the leases, rent roll and the underwritten revenue assumptions must be fully investigated and explained. The scope and results of the lease audit review must be discussed in the Underwriters Narrative. The underwriter should retain a copy of the individual leases reviewed in their working papers, which may be subject to audit but should not be included in the Firm Commitment application submission.

E. The underwriter is responsible for the review and reconciliation of the third party reports and the results of the mortgage credit review and other due diligence.

F. Lender Due Diligence Certification: With each Firm Commitment package, the Lender must submit a letter signed by a person authorized to bind the Lender which certifies that:

1. The Lender has reviewed all in-house and third party forms/reports/reviews;
2. The preparer of the forms/reports/reviews is qualified as required by this Guide and has any of the required insurance coverages;
3. The forms/reports/reviews were prepared in the manner required by the Guide and are complete and accurate; and
4. The proposed loan represents an acceptable risk to the Department and is financially sound, based upon the Lender's review and analysis, and that the application complies with all HUD statutory, regulatory, guidebook and administrative requirements.

G. HUD Forms Submission. The Lender must prepare a Master HUD-92264 signed by the Lender's underwriter. The third party contractors' HUD-92264 forms must be referenced and attached if they do not sign the Lender's Master form. Any variations between the Master HUD-92264 and the individual contractors' HUD-92264 must be identified and justification for the variance provided. The Lender must certify that all parties preparing forms, reports or reviews are qualified as required by the Guide.

11.2 HUD Hub/ PC Underwriting Review

A. Pre-application. HUD field staff should advise the Lender of any market or environmental concerns if not identified at the Concept meeting. If the Team Leader determines that the submitted exhibits in support of the pre-application are incomplete but can be cured within a short time, the Lender may have five business days to correct the deficiencies. HUD field staff will perform a completeness review within five business days of receipt of the complete application exhibits. When the Team Leader has determined that the pre-application exhibits are complete, the

Team Leader will assign the exhibits to the HUD technical specialists including EMAD. The format for the technical specialist review is in the Appendices. Upon completion of the technical reviews of the submitted materials, including the list of Lender reviewers and their qualifications, the Team Leader will prepare a memorandum to the Hub/PC Director that will summarize the results of the technical reviews, reconcile any inconsistencies, and recommend whether to invite a Firm Commitment application. If the Team Leader rejects or modifies the recommendation of a technical reviewer, it should be noted in the memorandum. If the Hub/PC Director concludes that an application should be invited, the Team Leader will prepare an Invitation Letter (See Appendix 4C) including any conditions. If a transaction requires review and approval by a Hub or National Loan Committee before an invitation letter may be issued, the Hub Director will request the appropriate loan committee's approval to proceed. If the Hub/PC Director concludes that an application should not be invited, or that there are issues that need to be resolved before an application can be invited, the Team Leader will prepare a letter to the Lender explaining why an application was not invited.

B. HUD Reviews, Signatures and Certifications. Upon determination of the acceptability of the application for processing, the HUD reviewers should sign their individual technical reviews and, when determined acceptable for processing, the Master HUD-92264 prepared by the Lender. The Master HUD-92264 summarizes the key technical processing conclusions which, along with the HUD-92264-A, will be the basis for the Firm Commitment.

HUD technical reviewers, Team Leaders and Hub/PC Directors should sign the HUD-92264 attached to the Firm Commitment. If a HUD technical review does not concur with the conclusions approved by the Hub/PC Director, they may document their non-concurrence separately in the file. The Team Leader should address the non-concurrence and document how the issues were addressed in the loan approval decision.

C. Underwriting Recommendation. The Team Leader will coordinate the technical reviews, resolve any inconsistencies and make a recommendation as to whether an application should be approved, modified or rejected and must document and justify any recommendation to approve a loan or to require conditions with which one or more technical reviewers non-concurs.

Upon completion of the technical reviews and the environmental assessment, the Team Leader will prepare a memorandum to the Hub/PC Director summarizing the individual reviews of the specialists, any proposed waivers of Guide requirements and the Team Leader's overall recommendation. The memorandum will specifically address:

1. The adequacy of the initial operating deficit for any new construction or substantial rehabilitation loans;
2. The adequacy of the 2% working capital escrow and 2% working capital construction contingency escrow for any new construction or substantial rehabilitation loans;
3. The adequacy of the initial deposit and ongoing reserve for replacement;
4. A description of any non-critical repairs to be performed after closing for Section 223(f) loans;
5. In a tax credit transaction, the schedule of the equity contribution at closing and remainder during construction;
6. The architectural drawings and specifications; and

7. Any environmental conditions or other concerns.

   Attach to the memorandum the Signature list and Previous Participation Certification from APPS, the technical staff reviews, the Lender narrative summary, the Lender's technical reviews. If recommended for approval, attach a proposed Firm Commitment with Forms HUD-92264 and HUD-92264-A signed by the HUD reviewers and Team Leader. Where the Team Leader has rejected a conclusion by the reviewer, or has modified any technical recommendation by the Lender or HUD reviewer, documentation and justification must be included in the memorandum. Note: HUD's review appraisers have the option to modify appraisal conclusions internally or to return the application to the Lender for revision of the appraisal. Should the HUD review appraiser choose to modify the appraised value, rent or expense conclusions internally, as per USPAP Standard 3, this opinion becomes its own appraisal whether it concurs with the opinion of value in the work under review or differs from the opinion of value. See Chapter 7 Section 7.11 for more detail.

D. Firm Commitment Decision.

1. After the Hub/PC Director reviews the memorandum and backup documentation, and any required loan committee approval is obtained, the Director will issue the Firm Commitment and sign the Forms HUD-92264 and 92264-A. If the Director overrides the recommendation of the Team Leader, or modifies any technical recommendation by the Lender or any HUD reviewer, the Director's decision and justification for it must be documented in the file. Lenders can appeal any rejections/modifications to the Hub Director. If a further appeal beyond the Director is necessary and appropriate, the appeal should be sent to the Director of Multifamily Development in HUD HQ.

   The Firm Commitment will identify the principals of the borrowing entity who have been approved to sign the exceptions to non-recourse in the Multifamily Loan Documents. Firm Commitments will be issued for a term of 60 days, and the Lender has the option of requesting an extension of the Commitment to prepare for the Initial Endorsement submission. The Hub Director may grant two 60-day extensions (or one 120-day extension).

   When the Hub Director determines that extenuating circumstances justify a limited extension of an outstanding Firm Commitment, the Lender must certify and Hub Director must concur that the documentation provided by the Lender demonstrates that granting the extension will not likely change the underwriting data and assumptions on which the Firm Commitment was issued or undermine the feasibility of the project due to a change in the market, inflation or other factors impacting cost. A change in the interest rate or other terms or conditions of the Firm Commitment may require reprocessing and amendment of the Firm Commitment.

   If a Firm Commitment has been extended beyond 120-days from its original date, the Lender must provide updated appraisal/market study, cost and mortgage credit, or other information as required by the Hub or PC for review prior to loan closing.

   Note: Only the Hub Director, Hub Operations Director or PC Director are authorized to sign Firm Commitments or endorse Insured Mortgage Notes.

The Department has limited flexibility to permit the resubmission of rejected applications. In accordance with the procedures contained in HUD Handbook 4410.1 Rev-2, Project Fiscal Procedures will apply.

2. Early Start of Construction. Construction may not start before Initial Endorsement and recordation of the insured mortgage, except with the prior approval of the Hub Director. When a valid Firm Commitment is outstanding, this requirement cannot be waived.

E. Amended Commitments. An amended commitment bears the same date as the original commitment, followed by the date of the amendment, although the applicable regulations are those in effect on the original commitment issuance date. Most underwriting changes, such as changes in mortgage amount and/or interest rate, will be incorporated in letter amendments to the commitment.

F. Reissued Commitments. A reissued commitment will have its own date and will substitute for the originally issued commitment. A Lender which accepts a reissued commitment will no longer have rights granted under the original, or a previously amended, commitment. A re-issued commitment is required for:

1. Requests for reconsideration of an expired or terminated commitment;
2. Changes in project location;
3. Major changes in plans and specifications; and
4. Reprocessing to reflect changes in the MIP.

G. Waivers. The Hub Director may waive requirements of this Guide that are not statutory or regulatory except for the following:

1. Debt coverage ratios for all programs;
2. Loan to value ratios for Section 223(f) loans;
3. Loan to cost ratios for the 221(d) and 220 programs; or
4. Application exhibits required for pre-application submissions and Firm Commitment applications for specific programs, including documents required by the Guide sections, which may in some cases not be mentioned on the exhibit list, but are still submission requirements.

H. Processing stages (for Pre-application and Firm Commitment applications) and HUD review procedures.

1. The Hub Director will submit to the Director of the Office of Multifamily Housing Development all waiver requests requiring HQ approval as early as possible. Requests for regulatory waivers will take longer to process since they require review and concurrence from the Office of General Counsel and the Deputy Assistant Secretary for Multifamily Housing, as well as the approval of the FHA Commissioner. HQ will not consider waiver requests submitted directly by MAP Lenders.
2. Any waiver granted in connection with the proposed transaction must be documented in the field office docket and HQ docket, along with the Lender's request and field office request. Waivers granted by the Hub must be submitted, along with supporting documentation, to the

Office of Multifamily Housing Development attn: LQMD which will review all waivers granted to determine if changes to this Guide or the regulations are necessary.

I. Two Stage Processing.

1. Market rate Section 220, 221(d) and 231 applications must be submitted under two stage processing (i.e., including a pre-application submittal) and may not apply directly for a Firm Commitment application. The Hub Director may waive two stage processing and allow a direct to Firm Commitment application for properties in which the concept meeting yields strong evidences of the following:

   (a) Stable markets, capable HUD experienced Lender, mortgagor, general contractor, architect, and management agent and that there are not environmental issues, or

   (b) A stable occupied market rate substantial rehabilitation property that, during the rehabilitation period, will not have:

      (i) major rehabilitation or unit reconfiguration,

      (ii) resident displacement except for short periods during interior rehabilitation of a unit,

      (iii) a reduction in current occupancy levels, or

      (iv) negative cash flow.

   (c) A pre-application letter that has recently expired, but delays prevented submission of the Firm Commitment application within the allowed time frames, and the Hub Director agrees that the application, the market data and the due diligence has not fundamentally changed.

2. Affordable properties or those with 90% or more rental assistance units may submit a Section 221(d) (4) application directly for Firm Commitment.

J. Limitations on Cost Not Attributable (CNA). Only in those instances where it can be documented that the project will produce affordable housing through the use of bond financing, tax credits, tax abatement, CDBG, HOME, HOPE VI, or similar local funding programs.

K. The Early Start of Construction requirements are contained in Chapter Section 5.7.

L. Certifications. The following Review Certification must be included by the Lender with the Underwriting Narrative:

I understand that my (appraisal, market study or architectural, cost, mortgage credit, valuation review) will be used by _____ (name of MAP Lender) to document to the U.S. Department of Housing and Urban Development that the MAP Lender's application for FHA multifamily mortgage insurance was prepared and reviewed in accordance with HUD requirements. I certify that my review was in accordance with the HUD requirements applicable on the date of my review and that I have no financial interest or family relationship with the officers, directors, stockholders, or partners of the Borrower, the general contractor, any subcontractors, the buyer or seller of the proposed property or engage in any business that might present a conflict of interest.

I am employed full time by the MAP Lender (underwriter) or under contract for this specific assignment (appraiser, market analyst, cost architect) and that I have no other side deals,

agreements, or financial considerations with the MAP Lender or others in connection with this transaction.

_____ Signature

Warning: Title 18 U.S.C. 1001, provides in part that whoever knowingly and willfully makes or uses a document containing any false, fictitious, or fraudulent statement or entry, in any manner in the jurisdiction of any department or agency of the United States, shall be fined not more than $10,000 or imprisoned for not more than five years or both.

11.3 Program Closing Provisions

This Section will address various program closing provisions and procedures that the Lender must be aware of to prepare for initial closing, final closing and initial/final closing events.

11.4 Loan Fees

A. Loan Fees. As provided in Section 3.2(I), loan fees may not exceed 3.5% of the mortgage loan amount, or 5.5% of the mortgage loan amount for transactions with tax-exempt bond financing.

B. Loan fees, if any, are earned are as follows:

1. Construction loan fees are earned at initial closing, except to the extent that the loan documents defer a portion to a later date. Construction loan extension fees are not earned until the time such extensions are granted.
2. Permanent loan fees and permanent loan extension fees, to the extent a separate permanent loan is anticipated, are earned at final closing.
3. Construction/Permanent loan fees (for construction loans anticipated convert to permanent loans) are earned at initial closing, except to the extent that the loan documents defer a portion to a later date.

C. Excess mortgage proceeds may be used after initial closing to pay permanent loan discounts, including those for construction/permanent loans and construction and permanent loan extension fees to the extent recognized by HUD under form HUD-92434M, paragraphs 20(b), (c), (d) and (g), if loan documents approved by HUD provide for the payment of such fees after initial closing, subject to the following:

1. Lender is required to escrow sufficient funds on Borrower's behalf to cover fees approved in form HUD-92434M, paragraphs 20(b), (c), (d) and (g), for payment after initial closing.
2. Borrower is required to furnish a written acknowledgement to HUD that any disbursements from the escrow accounts require HUD's advance written approval. Lenders must provide a separate escrow account for each escrow, as needed, as well as a separate letter for each disbursement from the various escrow accounts.
3. A Letter of Credit will not be accepted at initial closing for any of the amounts to be satisfied from excess mortgage proceeds.

4. Such escrowed excess mortgage proceeds may be released when earned.

D. Deferred Fee Collection. Section 8.14.D.4 sets forth provisions for the deferred collection of fees in connection with tax-exempt bond financing.

E. Broker's Fees.

1. Referral fees are always prohibited.
2. Lender may not pay anything of value directly or indirectly to any person or entity in connection with an insured transaction if the person or entity has received any other compensation from Borrower, seller, builder or any other person for services related to the transaction, or related to the purchase or sale of the mortgaged property, except as approved by HUD.
3. The Hub Director may approve compensation for services actually performed, which approval must be in writing and be based on the following findings:
   a. The service performed is necessary,
   b. The service is actually rendered,
   c. Payment is reasonable and customary,
   d. The broker's fee is included in form HUD-92434M, and
   e. Borrower submits a letter to HUD identifying the fee paid, the name of the broker, the reasons why it was necessary to employ a broker, and certifying that there is no identity of interest between Borrower/Sponsor and the broker, or between Lender and the broker.

11.5 Title Matters

A. Air Rights and Other Shared Interest Projects

1. A three dimensional air rights map for air rights projects is required. The existence of adequate vertical ways to the ground for required services, e.g., utility and fire suppression lines, chimneys, trash chutes, elevators and emergency exit stairs must be verified. In addition, there must be an acceptable discharge to a public way from all building egresses, including emergency exits, and services, e.g., trash removal.
2. Maintenance, joint use, easement and other agreements may be required. In cases where common facilities exist between the insured parcel and an adjacent parcel, Mortgagor must provide for recordation of an agreement for the common use land and facilities, e.g., common drives, common lobbies, elevators, walkways, utility roads, parking structures, recreation facilities, storm water management facilities (retention ponds detention ponds, swales and culverts) or other air rights project common facilities. The agreement must grant rights to the HUD project site and its residents to use the common facilities. If the HUD project is subject to property/homeowner association documents such as with a cooperative, these documents may provide for maintenance, access and cost sharing.
3. The Hub Director must:

a. Assure that the integrity and maintenance of air rights platform foundations and other structural members are defined as the air rights provider's responsibility.

b. Verify that shared maintenance/operating costs are equitable and that enforcement rights protect the project interests.

c. Require easements, cross easements or other documents to provide the HUD project and its residents the right to use the common facilities.

11.6 Mortgagor Entity's Organizational Documents

A. Mortgagor Entity's Organizational Documents

1. General. Organizational documents for the mortgagor entity are required to be submitted at closing. The specific documents required for each type of mortgagor entity are set forth in the FHA Housing Closing Guide checklist. These requirements apply to all types of closings including initial, initial/final, and final endorsements. For multi-tier entities, mortgagor entities will also be required to submit organizational documents for the tier at which Multifamily Hub staff has determined ultimate control over the day-to-day operations of the project resides.
2. Terms. The documents must expressly state:
   a. That the duration of the mortgagor entity is at least ten years longer than the term of the FHA-insured mortgage.
   b. That the terms of the HUD Regulatory Agreement take precedence in the event of any conflict with the terms of the organizational documents.
   c. That the mortgagor entity has authority to enter into the transaction and to comply with the requirements of the insurance program.
   d. That unless approved otherwise by HUD, the mortgagor entity is a single purpose-single asset entity.

11.7 Mortgage or Deed of Trust Note

A. Term. The term must be the same as specified in the firm commitment, as long as the maximum and minimum terms set out in the commitment meet the following requirement:

1. Generally, for most new construction or substantial rehabilitation rental projects, the term, calculated from the date of completion of construction, may not exceed the lesser of 40 years or 75% of the project's remaining economic life.
2. For existing projects (insured under Section 207 pursuant to Section 223(f)), the term must be not less than 10 years, and may not exceed the lesser of:
   a. 35 years, or
   b. 75% of the estimated remaining economic life of the physical improvements.
3. For 223(a) (7) projects, the term of the mortgage may not exceed the remaining term of the

existing mortgage. However, the Hub Director may approve a term up to 12 years beyond the remaining term of the existing mortgage if it is determined that the longer term is necessary to ensure the economic viability of the property and reduce the possibility of an insurance claim.

B. Prepayment Provisions. Except as specifically permitted below in Sections 11.7.B.3, B.4, and B.5, and subject to the conditions in Section 11.7.C, the Note must contain the following prepayment provisions:

1. Proprietary (For-Profit) Facilities.
   a. Prepayment must be permitted in whole or in part so long as 30 days advance written notice is given to Lender of intent to prepay, except as provided in Section 11.7.B.5.
   b. Prepayments must be permitted for up to 15% of the original principal amount in any one calendar year without a prepayment charge. Prepayments exceeding 15% may be subject to a reasonable charge agreed to by Mortgagor and Lender and included in the Mortgage.
2. Nonprofit Facilities.
   a. Without the prior written consent of the Commissioner, the mortgage debt may not be prepaid in full.
   b. The Commissioner may approve partial prepayments to reduce succeeding monthly payments over the remaining portion of the original mortgage term.
   c. The Commissioner may also approve partial prepayments made after 30 days written notice. Prepayments exceeding 15% of the original principal amount may be subject to a reasonable charge on such excess as agreed to by Mortgagor and Lender and included in the Mortgage.
3. State and Local Bond-Financed Projects. Subject to compliance with Section 11.7.C, projects funded from tax-exempt or taxable bonds issued by State or local governmental bodies may include the following prepayment restrictions and prepayment penalty charges in place of those contained in the printed HUD form of the Note:
   a. Prepayment restriction period (lockout) must not exceed 10 years plus the construction period stated in the construction contract, or, in the alternative, must not exceed 10 years from the commencement of amortization, and
   b. Prepayment penalty may be charged after expiration of the lockout stated in Section 11.7.B.3.a, provided the charge:
      (1) During the first year following the lockout does not exceed 5% of the original mortgage,
      (2) Declines on a graduated basis (to the extent practicable, the decline in the penalty percentage should be the same each year), and
      (3) Does not exceed 1% at the end of the fifth year following the lockout.
4. Other Bond Obligations or GNMA Mortgage-Backed Securities. "Other bond obligations" refers to any agreement under which Mortgagee has obtained the mortgage funds from third party investors and has agreed in writing to repay such investors at a stated interest rate and in accordance with a fixed repayment schedule. Mortgages funded with the proceeds of GNMA Mortgage-Backed Securities or other bond obligations acceptable to HUD may include the

following prepayment restrictions and prepayment penalty charges in place of those contained in the printed HUD form of the Note, subject to compliance with Section 11-10.D. Mortgages containing both bond financing, other than state or local government, and GNMA Mortgage-Backed Securities also may be subject to both a lockout provision and a penalty charge. Such lockout and penalty provisions are as follows:

a. A lockout not to exceed 10 years plus the construction period stated in the construction contract, or in the alternative, not to exceed 10 years from the commencement of amortization; or

b. A prepayment penalty charge provided the charge:

(1) Does not exceed 10% at the end of the first year following the construction period stated in the construction contract or the commencement of amortization,

(2) Declines on a graduated basis, and

(3) Does not exceed 1% at the end of the 10th year following the construction period stated in the construction contract.

If the initial penalty is 3% or less the HUD override language in paragraph 3 below, is not required; the penalty can be as great as 10% if the override language is included; or

c. A combination lockout and penalty charge in which the foregoing lockout and penalty provisions apply, but <u>in addition</u>:

(1) The lockout period does not exceed 10 years plus the construction period stated in the construction contract, or in the alternative, 10 years from the commencement of amortization, and

(2) The prepayment penalty does not exceed 1% at the end of the tenth year following the construction period stated in the construction contract or commencement of amortization.

5. Other Mortgages: Prepayment lockout provisions are not permitted, except where required by statute or HUD regulations to hold certain types of rentals available, e.g., for Section 223(f). (For details see Section 3.9.G and the Note, Form HUD-94001M).

6. Deletion of Preprinted Provisions. Those prepayment provisions that are preprinted in the Note may be deleted when the Lender selects one of the foregoing alternative provisions.

C. Conditions for Including Lockouts and/or Penalties. Compliance with the following conditions is required when prepayment lockouts and/or penalties are permitted.

1. Rider to the Note. The following language must be included in the Note, allowing HUD to override the prepayment lockout and/or penalty provisions in the event of a default:

"Notwithstanding any prepayment prohibition imposed and/or penalty required by this Note with respect to prepayments made prior to _____, 20__, [<u>enter first date on which prepayments may be made with a penalty of one percent or less</u>] the indebtedness may be prepaid in part or in full on the last or first day of any calendar month without the consent of the mortgagee and without prepayment penalty if HUD determines that prepayment will avoid a mortgage insurance claim and is, therefore, in the best interest of the Federal Government."

2. Use of the above rider to the Note is a condition of permitting lockouts for the types of projects

described above as "State and Local Bond Financed Projects," Section 11.7.B.3, and "Other Bond obligations or GNMA Mortgage-Backed Securities," Section 11.7.B.4, and for prepayment penalties that initially exceed 3 percent in any project.

3. Lenders may add the following provision to the Note and to the Lender's Certificate:

   "HUD would consider exercising an override of a mortgagee's prepayment lockout and/or penalty provision only if the following conditions are met:

   "(a) The project mortgagor has defaulted on the insured loan and HUD has received notice as required by the regulations;

   "(b) HUD determines that the project has been experiencing a net income deficiency, which has not been caused solely by management inadequacy or lack of owner interest, and which is of such a magnitude that the mortgagor is currently unable to make required debt service payments on the insured loan, pay all project operating expenses and fund all required HUD reserves;

   "(c) HUD finds there is a reasonable likelihood that the mortgagor can arrange to refinance the defaulted loan at a lower interest rate or otherwise reduce the debt service payments through partial prepayment; and

   "(d) HUD determines that refinancing the defaulted loan at a lower rate or partial prepayment is necessary to restore the project to a financially viable condition and to avoid a full insurance claim."

4. Rider to the Request for Endorsement. The new Request for Endorsement, Form HUD-92455M (at Section D.5 (A)), requires the Lender to certify that in the event of a default during the term of the prepayment lockout and/or penalty (i.e., prior to the date on which prepayment may be made with a penalty of one percent or less), it will:

   a. Request a 3-month extension of the deadline prescribed by 24 C.F.R. Section 207.258 for filing a notice of its intention to file an insurance claim and its election to assign the mortgage;

   b. Assist the Borrower to arrange refinancing to cure the default and avert an insurance claim if HUD grants the requested (or shorter) extension of the notice filing deadline;

   c. Report to HUD at least monthly on any progress in arranging a refinancing;

   d. Otherwise cooperate with HUD in taking reasonable steps to avoid an insurance claim;

   e. Require any successors or assigns to certify in writing that they agree to be bound by these conditions for the remainder of the term of the prepayment lockout and/or penalty period; and

   f. Notify HUD of the delinquency where a payment is not received by the 16th day of the month in which it is due.

D. Late Charge Provisions. Lender may collect a late charge for the cost of handling delinquent payments, subject to the following:

   1. Charges must not exceed two cents per dollar of unpaid principal and interest that is more than 15 days in arrears.

2. Late charges must be separately charged to and collected from Mortgagor and cannot be deducted from any total monthly mortgage payment, or collected from any reserve escrow, residual receipts funds, or from any interest accruals thereto.

11.8 Final Closing Forms and Requirements

A. Guarantee Following Completion

1. Form HUD-92442M, Construction Contract documents, Lump Sum and Cost Plus, contain guarantees against any defects due to faulty materials or workmanship that appear within a period of one year following substantial completion (as defined in the Contract Article 3).
2. The general contractor must provide assurance of performance under such guarantee, as follows:
   a. Bond. If form HUD-92452M, Performance Bond-Dual Obligee, was used, no action is required, as it remains in effect for 2 years from the date on which final payment under the construction contract becomes due. As part of this assurance, the surety will be required to perform when the general contractor fails to refund any overpayment to Mortgagor, a requirement of Form HUD-92442M, Article 4, Construction Contract-Cost Plus.
   b. Cash Assurance. If form HUD-92450M, Completion Assurance Agreement, was used at initial closing, the remaining escrow funds may be released except for the following, which must be withheld and handled as stated below:
      (1) An amount equal to the sum paid the general contractor pursuant to either of the above forms of construction contract, less the actual cost of construction, as determined in the cost certification, which amount shall be refunded to Mortgagor; and
      (2) An amount equal to 2½% of the total amount of the construction contract, which shall be retained in an escrow for a period of 15 months from the date of completion.
3. The contractor's liability for such corrections is not limited to the amount of funds comprising the escrow.
4. In addition, the guarantee funds are to be kept separate from any escrow that may have been provided to assure completion of any incomplete construction items.

Chapter 12

Construction Period

12.1 Start of Construction

A. Start of initial construction is the date when contract work commences. It must be diligently pursued without appreciable delay between activities, includes site clearance and other preparatory site work.

B. Early start of construction may be authorized in accordance with early start procedures (see Section 5.7). Where it occurs:

1. A pre-construction conference is required before the start of initial construction;
2. Construction inspections and change orders must be done in accordance with this chapter;
3. Authorization of any insured advances cannot occur until the endorsed instrument is recorded at initial closing.

12.2 Pre-Construction Conference

A pre-construction conference is required for every project and must precede the initial start of construction, including early start of construction. The HUD Inspector usually conducts the pre-construction conference and should hold it at initial endorsement where feasible, with the major participants present. The pre-construction conference may be conducted by the HUD Construction Coordinator (or designate), if the HUD Inspector is unable to attend.

A. Required attendees:

1. Borrower's representative;
2. Borrower's supervisory Architect;
3. General contractor;
4. Major subcontractor(s);
5. HUD representative;
6. HUD mortgage credit analyst; and
7. Lender's representative.

B. Supplementary Conditions of the Contract for construction, Form HUD-92554M. The form must address Davis-Bacon wage rates, Federal labor standards and equal employment provisions, including:

1. Contract obligations of the general contractor and all subcontractors, including:
   a. Certification of compliance with Davis-Bacon wage rates with each request for advances.
   b. Davis-Bacon wage rates also apply to a second mortgage securing a governmental loan.
2. Statement of sanctions that may be imposed for not complying with the supplemental conditions.
3. Requirement that the applicable Davis-Bacon wage decision and the Form HUD-92554M must be made part of the subcontracts for all tiers.
4. Emphasize the importance of Federal wage payments, prompt certified payroll submissions and proper record keeping. Instruct that a copy of the applicable Davis Bacon wage decision and Form WH-1321, Notice to Employees, must be conspicuously posted on the job site.
5. Indicate who on the HUD labor relations staff will review for labor standards compliance and refer any further inquiries concerning Davis-Bacon wage and reporting requirements to that staff.
6. Give copies of the Equal Opportunity poster to the general contractor and the subcontractor(s) to post conspicuously at the job site.
7. Make available copies of HUD's Contractor's Guide to Davis-Bacon.

C. Contract Administration

1. Explain general contract administration, including responsibilities of the Lender, borrower, borrower's Architect, general contractor, and HUD representative.
2. Explain the procedures for:
   a. Change orders;
   b. Requesting construction document clarifications;
   c. Reporting and correcting non-compliant work;
   d. Requesting periodic payments and release of escrows;
   e. Substantial completion of work or portion thereof; and;
   f. Permissions to occupy, including management plans and rent rolls.
3. Stress that work changes completed in anticipation of a future change order will be regarded as non-compliant. There will be no insured advances for it or other work dependent on it.
4. Periodic advances. Explain:
   a. Borrower's and general contractor's required preparation of requests, including the field approval and subsequent processing;
   b. Provisions for submitting surveys, title reports, and other documentation in support of construction advances;
   c. Requirements for contractor's retainage and its release.

5. Stored materials. Explain procedures to request payment for materials stored onsite, and components stored offsite where applicable. (See Appendices 12B and 12C)
6. Offsite work. Explain procedures to request payment for completed offsite work, the required retainage and its release.
7. Termination of contract(s). Discuss provisions for terminating the construction contract and/or Architect's contract, and the Lender's responsibilities during the construction stage and in the event of a default.

D. Cost Certification

1. Summarize cost certification requirements for the mortgagor and (if applicable) the general contractor, subcontractors, equipment lessors and suppliers, and industrialized housing manufacturers. Where there is a second mortgage securing a Governmental loan, advice that cost certification also applies to the second mortgage.
2. Inform all parties that a pre-cost certification conference will be held when construction is 90% complete and that detailed instructions will be provided at that point.
3. Stress that:
   a. Identities of interest that develop or become known after initial closing must be reported to the Lender and to HUD within 5 working days of having such knowledge;
   b. HUD must give prior approval for all identity of interest subcontractors and apply penalties where this is not done;
   c. Self-owned equipment must be certified; and
   d. Paper conduits are prohibited.
4. Clarify the 50/75 percent rule (see Section 13.15).

12.3 HUD Construction Monitoring

A. Purpose of Inspection.

1. Inspection means the periodic observations made of rehabilitation/ construction at the site of a multifamily housing project by a HUD representative (inspector) for the purpose of protecting HUD's interests. Inspections are made to evaluate the contractor's and Architect's performance, to obtain construction in accordance with the contract documents, and to report on conformance with prevailing wages and other contract requirements.
2. The instructions for inspection are the same for projects involving the insurance of advances and those to be insured upon completion, except for those variations specifically stated to be applicable to one or the other.

B. Access. At all times, HUD has the right of access to the property and the right to inspect all work performed and materials furnished to complete the project.

C. HUD Construction Manager's/Coordinator's duties. The HUD construction manager (CM) or architectural designee is responsible for the proper performance of all functions relating to inspection, as well as the instruction and supervision of all HUD personnel involved. The CM must be kept informed of the general progress of the work on all projects during the construction stage and guarantee period and must be familiar with the problems involved.

1. Assignment. The CM will assign either a HUD construction analyst or a contractor to inspect a project before the start of construction. The person inspecting the project may be a Design Representative, a Construction Representative, or a person or group hired by HUD to do the inspections, referred to as an "inspector." The CM will select the inspector on the basis of competency with regard to the scope of the project and to the type of construction involved. Several projects being constructed concurrently may be handled by one inspector. Only in very unusual circumstances will an inspector be assigned full time to any one project. Upon assignment, the CM will issue to the inspector the following:

   a. Set No. 3 of the contract drawings and specifications. This set becomes the HUD as built set for the inspector to conform it to the contractor's "Record Set."

   b. Copy of the construction contract. The required Contract for insured advances is the HUD Construction Contract, HUD-92442M, which contains alternate provisions for cost plus and lump sum contracts. The form may or may not be used in insurance upon completion cases, but a construction contract in some form is required and must be furnished to the inspector.

      (1) Form HUD-92442M, Construction Contract-Lump Sum, may be used when there is no identity of interest between the borrower and the contractor.

      (2) Form HUD-92442M, Construction Contract-Cost Plus, may be used in any case, and shall be used when there is an identity of interest between the borrower and contractor.

   c. Owner-Architect Agreement, AIA Document B-108, when an Architect is required to administer the construction contract.

   d. Contractor's and/or borrower's cost breakdown - Schedule of Values, Form HUD-2328 when insured advances are involved.

   e. Drawings and specifications pertaining to off-site improvements.

   f. Agreements or contracts providing for off-site construction.

2. Field Supervision. The CM shall keep informed of the general quality of inspections and the performance of inspectors by maintaining close contact with their work through job site visits. A regular routine for supervising field operations should be established and followed. Required methods of field supervision follow:

   a. A minimum of one (or more where appropriate) field review inspections shall be made on each project to evaluate the performance of the HUD inspector. Field review inspections shall be recorded on a HUD Representative's Trip Report, Form HUD-95379.

b. Construction should be field reviewed where the use of questionable methods of construction, materials, uncorrected non-compliance, or other problems are reported.

c. Projects should be field reviewed at construction stages where problems have occurred in that jurisdiction.

3. Office Review. The CM shall review all Trip Reports, Forms HUD-95379, completed by the HUD inspectors. If the reported conditions indicate the necessity for desirability of field review or other special handling, appropriate action shall be initiated.

   a. Review should not be restricted to the entries on the report. The absence of significant evaluation comments may, under certain circumstances, indicate desirability of field review.

   b. The CM should be aware of progress, trends, new or uncorrected non-compliance, unusual conditions, etc., in order to be familiar with the work and to initiate any required corrective action immediately.

   c. The inspector shall be advised of any unsatisfactory action or detail in the report, or any error in its preparation, so that similar mistakes will not occur in the future.

4. Training.

   a. Inspection conferences shall be held when deemed necessary by the CM. The purpose of the conference is to maintain and improve the quality and efficiency of the construction observation function.

   b. Field and office review of inspections will indicate individual training needs and subjects for discussion at inspection conferences.

   c. It is essential that new inspectors and new staff be trained in the field as well as in the office.

5. Construction progress meetings. During construction, the contractor, mortgagor, mortgagor's supervisory Architect and the HUD inspector must attend monthly job meetings at the job site when a monthly request for advances are prepared.

   a. The owner's representative must be a member of the borrower entity, usually a general partner. Nonprofit organizations may be represented by a member of the Board of Directors.

   b. The HUD Inspector must:

      (1) Comment to the group on the quality of construction and of the Architect's observations and the contractor's supervision.

      (2) Comment on all known construction defects and deficiencies (non-compliance) and methods of correction.

      (3) Explain that changes in the work from the contract documents (non-compliance) must be resolved by approved change order requests or the work done in accordance with the contract documents.

(4) Inform parties of HUD policy for holdback of construction advances until non-compliance is corrected.

(5) Record on Form HUD-95379 the issues raised at the meeting. Significant concerns of any party should be presented by memorandum through the CM to the Hub Director.

c. Monthly meetings may also be used to resolve equal opportunity and labor disputes. When such disputes are known, the HUD Labor Relations and Equal Employment officers must be invited to attend.

D. Inspector's Duties. The inspector is a HUD representative, not a superintendent for the contractor or "clerk of the works" for the owner or Architect. The inspector, as HUD's agent, must endeavor in a tactful, helpful and courteous manner to obtain construction that conforms to the drawings, specifications, and sound construction practice within the scope of the contract. The inspector must be factual and specific in all statements in reporting and recording significant construction developments observed.

1. Orientation. Upon assignment to a project, the inspector will study the drawings and specifications and become familiar with the conditions at the site. If, during this examination or during construction, any nonconformity with HUD requirements or site conditions not considered in the design are found, they are to be reported by memorandum through the CM to the Hub Director. The Hub Director will work with the Lender, owner, contractor and other related parties to resolve the noncompliance.
2. Facilities. The contractor must furnish the inspector with enclosed working space that is acceptable to HUD. Adequate, but not elaborate, facilities should be required as soon as actual construction begins at the site.
3. Inspections. The inspector shall make at least two job site visits each month. Additional visits may be necessary due to the nature of the project. The frequency of inspection should assure reasonable continuity and recognize the size and character of the project, the speed with which construction is progressing and the quality of work on the project. Visits should be scheduled to observe major construction operations without neglecting lesser operations. Sufficient time must be allotted to each visit to make a complete inspection.
   a. The major functions during inspection are to: Evaluate the construction supervision of the contractor and contract administration of the Architect; report on occupancy, delays, disputes, and changes; report noncompliance with the contract documents observed by the inspector and/or the supervisory Architect; determine that the amounts requested by the contractor and recommended by the Architect for payment are reasonable; conduct employee wage interviews using Form HUD-11; and report on labor and EEO compliance.
   b. Each inspection shall be recorded on a HUD Representative's Trip Report, Form HUD-95379.

c. Reporting requirements. The following documents executed during inspection must be promptly sent to the CM, the project Architect and the Lender's Construction Loan Administrator:

(1) HUD Representative's Trip Report, Form HUD-95379:

Original to the CM, with copies to the Architect and the Lender's Construction Loan Administrator.

(2) Contractor's Requisition, Form HUD-92448:

Original to the Lender's Construction Loan Administrator for signature with copies of the signed document to the CM, the Architect and the HUD inspector.

(3) Change Order Form HUD-92437:

Original to the Lender's Construction Loan Administrator for signature with copies of the signed document to the HUD CM, the Architect, and the HUD inspector.

(4) Permission(s) to Occupy, Form HUD-92485:

When all required signatures (mortgagor, architect, and contractor, mortgagee, and HUD inspector) are affixed, the document will be sent to the HUD CM for approval. Upon signing by the FHA authorized agent, copies are sent to the Lender's Loan Administrator, the Architect, and the HUD inspector.

4. Start of Construction. The inspector will report the date of initial construction start and the date of the start of permanent construction on Form HUD-95379.

a. The date of the initial construction start, used for recording and reporting purposes, is the "start of construction" as used in connection with labor standards and prevailing wage requirements. This is defined as the beginning of initial site clearance and preparation, provided these activities are pursued diligently and are followed, without appreciable delay, by other construction activities.

b. The date recorded as the start of permanent construction, used for the purpose of determining the earning of the inspection fee, will correspond to the first day that permanent on-site building elements were put into place, such as footings and/or foundations, pilings, utility lines, etc.

c. While excavation is an integral part of foundation work, it does not constitute a start of permanent construction.

5. Unified Report. At the beginning of construction, the inspector should consult with the HUD Design Representative and the CM in regard to the need for inspection of the project by HUD technical specialists. Any differences of opinion between the inspector and the technical specialist in regard to project construction will be resolved by the CM. The inspector must submit a unified inspection report to the Architect and the Lender.

6. Shop Drawings and Other Data. During the construction period, the inspector must check whether shop drawings are being submitted by the contractor for approval by the Architect as required by the AIA General Conditions of the Contract. Upon request by the Architect or the

inspector, the contractor will keep copies of tests, certifications and any other data required by the contract documents onsite for review.

7. Off-site Fabricated Construction. If off-site fabricated construction components are involved, the CM will determine if there is a need for inspection at the factory to determine acceptability. If the manufacturing facilities are outside of the jurisdiction of the HUD Office and inspection is essential, the CM will submit pertinent drawings and specifications, together with a request to the Hub Director to have the inspection made by the HUD Office located near the factory.
8. Distribution. If an Architect is not required for contract administration, then where these instructions require the HUD inspector to submit findings to the Architect, they are to be submitted to the contractor.
9. Work Stoppage. The HUD inspector will report to the CM on Form HUD-95379 any work stoppage unless such stoppage is due to inclement weather or similar reasons. If known to the inspector, the reason for the work stoppage should be stated and when resumption of construction is anticipated.
10. Occupancy. The HUD inspector will complete the portion, "FHA Inspection Report," of Form HUD-92485, Permission to Occupy, when submitted, to request permission to rent or occupy specific living units, commercial or other space. The Form is to be submitted when the inspector reports safe ingress and egress to the units and/or building, as evidenced by a certificate of occupancy from the locality. Units and spaces should not be occupied prior to approval by HUD. The Hub Director and MAP Coordinator should determine who in the Hub or PC will approve the permission to occupy.
    a. Occupancy prior to the execution of Form HUD-92485 will be reported to the Hub Director by written memorandum.
    b. The inspector will also include on the Form HUD-95379, the number of units occupied prior to approval, as well as the date occupancy took place.
11. Additional duties of the `inspector:
    a. Advises the Architect administering the construction contract on HUD requirements;
    b. Reviews the Architect's job log;
    c. Reviews copies of the Architect's decisions;
    d. Reports on project construction progress to the CM on Form HUD-95379;
    e. Notifies the Architect and the contractor if an identity of interest exists between the owner and the contractor, or if it is determined that there are any essential variations in the cost of the work installed, materials stored and the request for construction advances recommended by the Architect; and
    f. Conducts interviews with an appropriate sampling of the laborers and mechanics engaged and records interview information on Record of Employee Interview, Form HUD-11, in connection with wage and labor compliance in the construction of the project.
12. Construction record. From the initial construction start through final inspection, the inspector shall be responsible for maintaining a record of construction that includes minutes of the pre-

construction conference as well as reports of required guarantee inspections. The inspector shall keep a record binder when the CM first assigns the project or may elect to expand the project record binder to include inspection reports. All forms, reports, decisions and documents relevant to construction or inspection reporting shall be recorded in the binder in chronological order. The journal shall be on the left side of the binder and forms and documents on the right. The forms and documents listed below shall be included in the Construction Inspection Record Binder, when applicable.

a. Drawings and specifications: Sets 1, 2, and 3 referenced in journals though filed elsewhere (record the storage location of set 1 and use of 2 and 3).

b. Off-site drawings and specifications (referenced in journal).

c. Construction Contract, Forms HUD-92442M.

d. Owner-Architect Agreement.

e. Progress schedule.

f. Contractor's and/or Borrower's Cost Breakdown, Form HUD-2328.

g. HUD Representative's Trip Report, Form HUD-95379.

h. Contractor's Requisition, Form HUD-92448.

i. Change Orders Form HUD-92437, AlA G710, and Architect's supplemental instruction or equivalent.

j. Letters, memoranda, notes, and worksheets.

k. Journal of Architectural Actions (if separate binder).

l. Surveyor's Report, Form HUD-92457M (final and others, if requested).

m. Permission(s) to Occupy, Form HUD-92485.

n. Record of established escrows including amounts escrowed and a complete list of unfinished construction items, record of call back inspections and recommendations for monies to be released.

13. Projects of Insurance Upon Completion. The inspector will report the percentage of completion of the project on Form HUD-95379 at the end of each month. This percentage is an approximation for general information and is not used for disbursement.

14. Off-site inspection. The inspector checks all off-site construction for conformity with the terms of the contract and reports work progress by percentages on Form HUD-95379. Completion is reported on Form HUD-92464.

E. Reporting and dealing with serious construction problems. HUD Offices must identify and report, by electronic mail, to the Hub Director and the HUD Office of Lender Qualification and Monitoring Division all insured multifamily projects under construction or in the guarantee period that have serious construction defects or other serious construction related problems. This information will be used to reply to inquiries, as an "early warning system" on troubled projects, and to determine if assistance by the HUD Office is necessary.

1. The inspector must identify all construction problems that may delay completion or lead to foreclosure or assignment of the mortgage to HUD by using Form HUD-95379, HUD Representative's Trip Report.
2. The CM must prepare a referral memorandum to the Hub Director when:
   a. Work stops for 20 calendar days;
   b. There are slow payments or non-payments to the general contractor and/or subcontractors;
   c. Contractor abandons the job;
   d. Contractor, owner or Architect changes during construction:
   e. Correction of any construction deficiency is not started within 30 days of the first notification to the contractor; or
   f. Contractor can't or won't correct any construction defect or latent defect.
3. The referral memorandum must include full details of the construction related problem, including:
   a. A copy of Form HUD-95379, which identifies the problem.
   b. The inspector's opinion of the cause and recommendation for correction.
   c. A report of action by the CM and/or other HUD Office staff.
   d. A report of actions by the owner, Architect, contractor, mortgagee and bonding company (when appropriate).
   e. A plan of action to be undertaken by the HUD Office if the mortgage is assigned to HUD during construction or foreclosure is initiated by the Lender.
4. Only the initial report is required unless the Hub Director requests further action or follow-up by the HUD Office.
5. For complete instructions on handling problems before final closing, see Appendix 13D.

12.4 Architect's Duties in Administering Construction Contract

The Architect shall:

A. Provide services in accordance with the Owner-Architect Agreement.

B. Have no identity of interest with the owner or contractor. An identity of interest is defined in the HUD Amendment to the B108, Owner-Architect Agreement (see the MAP Forms Book).

C. Ensure that construction is carried out in accordance with the contract documents, including:
   1. Restrict materials, products and equipment to those specified.
   2. Restrict all deviations to those substantially consistent with the original design concept including form, color, and texture.

3. When arriving at the net amount due on every requisition, compare the cost of the work and materials with the cost to complete the project. Current and previous payment must relate to the total cost for completion.
4. Restrict substitution of items of a different design or size from those specified to those that are equivalent in utility (i.e., durability, quality, and ease of maintenance).
5. Restrict substitution of any material differing in composition or appearance from the one specified to one which is equivalent in its attributes (i.e., character, quality, durability and ease of maintenance).
6. Keep a log on the site that is readily available to the mortgagor and HUD representatives.

D. Architect's supplemental instructions. The architect administering the construction contract may issue field orders using AIA Document G710, Architect's Supplemental Instructions, or a similar form.

1. The architect must send a copy of each supplemental instruction to HUD, although prior approval by the Lender and HUD is not required.
2. Supplemental instructions must not involve a change in contract sum or contract time.
3. Supplemental instructions may be used to:
   a. Direct the contractor to bring construction into compliance with the contract documents.
   b. Interpret or clarify the contract drawings and specifications.
   c. Order minor changes in the work, not involving cost.
   d. Accept specified equivalents.
   e. Record other "field orders" that are not construction changes.

E. The Architect administering the construction contract is responsible for reporting in writing the results of periodic visits to the construction site. The Architect's log should provide information regarding assessment of the progress of the work and a record of the actions taken to insure that the work is being accomplished in the best interests of all the parties.

1. The American Institute of Architects (AIA) Document G711, Architect's Field Report, may be used for the log.
2. A log of each visit should show, at a minimum, the following:
   a. Date of inspection.
   b. HUD project identification and location.
   c. Time, weather, and temperature range.
   d. Estimated percent of completion.
   e. Work in progress and conformance with the contractor's progress schedule.
   f. Persons present at work site.
   g. Observations and items to verify.

h. Information or action required.

i. Firm name and signature.

12.5 Architect's Adequacy

The Architect's administration of the construction contract is covered by the Owner-Architect Agreement and by the General Conditions of the Contract for Construction, AIA Document A201. The HUD inspector is responsible for determining the adequacy of the Architect's administration, which determination will not be based just on the number of visits or the length of time spent by the Architect on the job, but on whether the construction complies with the contract documents based on the Architect's observations.

A. Deficient administration. If the Architect does not report all observed non-compliances with contract documents and unacceptable performances by the contractor and pursue all avenues to obtain compliance with the contract, then the Architect's administration of the construction contract will be considered deficient. The Architect will not be responsible for actual construction, construction means, methods, techniques or other related responsibilities of the contractor. However, on the basis of on-site observation as the owner's representative, the Architect must keep the Lender, owner and HUD informed of the progress of the work and endeavor to protect the owner and HUD against defects and deficiencies in the construction.

B. Reasons for termination of services. Inadequate performance, undue delay, misrepresentation or failure to act on the part of the Architect or the Architect's associates and employees shall be reason for the termination of the Architect's services on the project and may adversely affect the firm's acceptability on future projects.

C. HUD office actions. The HUD inspector shall bring to the attention of the Architect specific areas in which services are considered deficient. Sufficient time and appropriate assistance shall be given to obtain necessary compliance.

1. When the Architect's performance is first observed as deficient, in addition to the HUD Representative's Trip Report, Form HUD-95379, the inspector shall also prepare a written memorandum to the CM of the deficiency and advice of any planned actions or assistance. The memorandum should recommend that future requests for Architectural inspection fees be disallowed until performance improves to an acceptable level.
2. An immediate follow-up by the CM is always required. Conferences with the inspector and the Architect should be arranged and a target date established for the Architect to obtain compliance. The CM shall inform the Hub Director of current problems and of established target dates for corrections. Deficiencies related to misrepresentation, undisclosed identity of interest and known illegal kick-backs should be immediately referred to the local HUD Office

of General Counsel with a copy to the Hub Director. The local HUD Office should clearly document all actions.

D. Request for contract termination. When compliance with the contract cannot be obtained within 30 days, the Hub Director shall request termination of the Architect's contract in accordance with the provisions of the Owner-Architect Agreement. Upon termination, the Architect shall be entitled to only the prescribed portion of the fee determined by the percentage to which construction was completed on the date that the Architect was removed from the project. The Hub Director has full authority to secure acceptable performance.

E. Contract termination. The owner will hire an independent Architect who is acceptable to all parties to continue the administration of the project construction documents. The HUD inspector does not assume the Architect's responsibility.

12.6 Completion Inspections

A. Substantial completion. The Architect will date and sign the certification on Form HUD-92485, Permission to Occupy, for that part or for all the work that is sufficiently complete, in accordance with the contract documents, and may be occupied for the use intended.

1. The contractor must submit a punch list of items to be completed or corrected to the Architect when the work is ready for occupancy. (See Article 9.8, AIA Document A201.)
2. The Architect will inspect, check the punch list and modify it if necessary, and determine when the work is substantially complete. (Dwelling units containing punch list items will not be accepted for occupancy. However, punch list items in interior common areas and on the exterior do not preclude occupancy.)
3. Certificate of Substantial Completion: The HUD inspector will verify on Form HUD-92485 the date that the work, or a portion of the work, is substantially complete and suitable for occupancy. Where the Owner/Architect Agreement and the General Conditions of the Construction Contract, AIA A201, refer to a Certificate of Substantial Completion, it confirms that the Permission to Occupy Project Mortgages, Form HUD-92485, was executed. The date of substantial completion of the project is the date that the HUD Representative signs the Permission to Occupy for the final building or for the portion of the work that is completed.
4. The Contractor’s Guarantee Period commences with Substantial Completion of the Project as defined in Article 3.B of the Construction Contract, HUD-92442M which takes precedence over AIA A201, Article 9.8.4, and stipulate that warranties commence with the substantial completion of each portion of the work.

B. Final completion inspection. The Architect and inspector will make the final inspection upon written request of the contractor, and may do so separately.

1. The Architect must determine that all punch list items have been completed unless they are beyond the control of the contractor (i.e.: items of delayed completion).
2. The inspector must prepare the final inspection report on Form HUD-95379 which includes:
   a. Reports onsite construction completion, although there may be items of delayed completion.
   b. Lists and describes any items of delayed completion.
   c. Lists any offsite work and reports the percentage of completion for each.
3. The HUD Construction Manager/Coordinator will check the final inspection report to determine:
   a. If unacceptable and, requires re-inspection (i.e.: the report is not considered final).
   b. If acceptable, the report will be endorsed as follows:
      (1) "Construction acceptably completed." (If there are items of delayed completion, add, "subject to escrow of funds to assure completion of listed items of delayed completion.")
      (2) "All offsite sewer, water, electrical and gas facilities are completed, connected and operable, and safe, adequate, all-weather ingress and egress provided." (If offsite item incomplete, add, "except as stated at the time of inspection.")
      (3) Date and sign the report.
   c. CM will prepare a memorandum for signature by the Hub Director transmitting the final inspection report, which:
      (1) States the date of final completion (i.e.: the date of final inspection);
      (2) Lists incomplete offsite work; and
      (3) Lists items of delayed completion and the estimated of cost of completion for each item.

      NOTE: The escrow for items of delayed completion must not be less than 150% of the estimate to complete and must not exceed 2% of the mortgage. Work must be completed within the time specified in Form HUD-92456M, Escrow Agreement for Incomplete Construction, but not more than 12 months from the date of the final HUD inspector's trip report.

C. Guarantee inspections. A minimum of 2 inspections will be made of all work to identify and, if necessary, require correction of latent defects (defective or nonconforming work not observed during construction) within 1 year of the date of final completion.
   1. The CM/Coordinator will schedule guarantee inspections as follows:
      a. The first inspection must be within 9 months of final completion and should provide for inspection of the entire project.

b. Other inspections may be necessary to assure inspection of seasonal items such as heating and landscaping.

c. The last inspection must be not later than the 10th day of the 12th month to check previously reported defects and their correction, and to identify any additional defects.

2. The inspector must report each guarantee inspection on Form HUD-95379, including:

a. If work is acceptable, state, "All observable work acceptable at the time of this inspection."

b. If unacceptable, list latent defects.

(1) Describe each item.

(2) Recommend method of correction.

(3) Estimate current cost of correction.

c. Check any item of delayed completion and list complete and uncompleted items under a separate heading.

d. Note any improper maintenance or casualty damage under a separate heading.

12.7 Insurance of Advances and Related Matters

A. General.

Insurance of advances is the process of releasing insured mortgage funds and other funds necessary for the construction, acquisition and/or refinancing of the project. The following general criteria apply to the advancing of such funds.

1. All escrowed funds for on-site improvements (with the possible exception of grant/loan proceeds furnished by a government agency or instrumentality or tax credit equity proceeds) must be disbursed before mortgage proceeds. See Section 8.10 for instructions on grants/loans and tax credit equity and Appendix 12A for instructions on the pro-rata disbursement of tax credit equity proceeds.
2. The amount of construction funds approved and advanced for insurance must be consistent with construction progress as approved by the HUD Field Representative.
3. Other mortgagable items must be supported with proper bills and/or receipts before funds can be approved and advanced for insurance.
4. The amount advanced for construction items must be adjusted for a 10% holdback until 50% completion.
5. The final amount approved for insurance must be supported by certified costs recognized in the cost certification review. Projects that are exempt from the cost certification process can submit a copy of their final Sources and Uses Statement prepared by the allocating State Housing Finance Agency for HUD's review of the final sources and uses amounts.
6. The Application for Insurance of Advance of Mortgage Proceeds, Form HUD-92403, is initiated by the mortgagor. The initial and final advances must be submitted by the mortgagor

to HUD for review and approval. Interim advances are approved by the mortgagor, based upon the HUD inspectors' approval of the construction amount. The approved Contract Administrator must sign forms HUD 92403 and HUD 92448 in the Authorized HUD Official signature block.

a. For the initial and final advances, the PC Director must sign Forms HUD-92403 and HUD-92448, in the following spaces:

(1) Under Authorized HUD Official for Form HUD-92403, and

(2) Under Director, Housing Development for Form HUD-92448.

b. For the interim advances, the Lender (by either the Lender's underwriter or construction loan administrator) must sign Forms HUD-92403 and HUD-92448 for HUD, in the same spaces as in 6.a (1) and (2) above.

7. Supporting materials to Form HUD-92403 include supporting bills/receipts and Form HUD-92448, Contractor's Requisition, if requesting construction funds.

B. Lender's role in processing HUD-92403 includes:

1. Complete the application indicating:

a. Amount requested by mortgagee;

b. Approximate disbursement date;

c. Amount to be advanced from mortgage proceeds;

d. Amount disbursed from mortgagee's front money escrow, if any; and

e. Total loan proceeds disbursed including the current request.

2. Submit the initial and final application to HUD for review and approval.

3. Process and approve interim advances.

4. Ensure clear title before advancing the approved disbursement.

5. Notify HUD in writing when clear title does not exist or is impaired.

C. Stages of Advances.

In cases involving insurance of advances, HUD and the Lender's processing of the advance is divided into the following stages:

1. Initial advance. Refers to the first application and coincides with the initial endorsement of the mortgage. The initial advance will be reviewed and executed by the HUD mortgage credit analyst. The Lender should submit Form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds, with supporting documentation for HUD approval.

2. Interim advances. Interim advances are subsequent applications up to completion of the project and will be processed and approved by the Lender.

3. Next to Final Advance. When HUD is in receipt of the contractor's certification and of the consent from the mortgagor, and surety, if any, the final 5% of the construction holdback is released.

Note: This procedure only applies to non-identity of interest contractors or where the contractor's identity of interest in the project ownership is less than 5%.

4. Final Advance. This refers to any remaining balance of mortgage proceeds at final endorsement and takes into consideration funds necessary to set up the escrows for "Items of Delayed Completion" and "To Be Paid In Cash Items" and will be processed by HUD. In addition to the Form HUD-92403, the Lender must submit a copy of Form HUD-92451 Financial Record of Mortgage Loan Transaction, which reflects releases to the various payees during the construction period.

D. Instructions for Approval of Initial/Interim Advances can be found in Appendix 12A.

E. Contractor's Monthly Requisition and Related Matters. See Appendix 12B for instructions on completing Contractor's Requisition, Form HUD-92448, and related matters.

F. Next to Final Advance. The final advance may be requested when construction is acceptably complete, even if there are items of delayed completion.

1. It may provide for the release of the contractor's holdback provided the conditions in Section 12.15.D have been met. The amount approved for release will be based on the cost certification review and HUD-approved amount, and will consider items of delayed completion.
2. The balance of the off-site escrow may be released provided:
   a. The off-site sewer, water, electrical and gas facilities are completely installed and connected; and safe and adequate all weather facilities for ingress and egress are provided.
   b. All other required off-site construction, if any, is completed.
   c. Otherwise, completion is to be assured by a cash deposit in an amount equal to 150 percent of the HUD estimate of the cost of such off-site construction.

G. Final Advance. The Application for Insurance of the Final Advance will request any remaining balance of mortgage proceeds and ensures that:

1. The mortgagor's cost certification has been approved and the maximum insurable mortgage amount determined using Form HUD-92580, Maximum Insurable Mortgage.
2. Form HUD-92403 is accompanied by a completed Form HUD-92448, with required Contractor's Prevailing Wage Certificate, if the contractor's holdback has not been previously disbursed. Refer to Section 12.15.D for instructions on releasing the contractor's holdback.
3. The sum to be approved for the advance is the balance of the mortgage proceeds, based on the maximum insurable mortgage on Form HUD-92580. Refer to Section 13.12 for instructions on an advanced amortization adjustment, if any.
4. Set up the escrow under the provisions of Form HUD-92456M, Escrow Agreement for Incomplete Construction (formally Escrow Deposit Agreement for items of delayed completion).

5. Form HUD-92023M, Request for Final Endorsement of Credit Instrument, or Form FHA-2453, Commitment to Insure Upon Completion, must have been submitted and reviewed.
6. Set up the escrow for the mortgagor's unpaid construction costs under the provisions of Form HUD-92476.1M, Escrow Agreement for Non-Critical, Deferred Repairs, (formally Escrow Agreement for Unpaid Construction Costs, Repairs or Needs Assessment Repairs).

H. Keeping the mortgage in balance.

Soft cost overruns such as interest, taxes, MIP, and insurance which result from delays before completion of the project and which are the fault of the general contractor, (i.e., due to poor performance), are to be funded from the liquidated/actual damages clause in the construction contract. This clause is not intended to penalize the contractor, but to provide a source of funds for the increased soft cost. When the interest allocation is near exhaustion (*e.g. when the balance after several draws is $1,000 or less*) HUD should be notified immediately. The Lender should ask the Architect and the HUD inspector to estimate an expected completion date, and should follow the following procedure:

1. When the interest allocation is near exhaustion, have the Architect and the HUD inspector estimate an expected completion date.
   a. Compute the minimum liquidated damages for the period between the completion date specified in the construction contract, as adjusted by approved change orders, and the estimated completion date.
   b. When the interest allocation has been exhausted, the nonprofit developer's fee, if applicable, or the working capital escrow should be used to keep interest current.
   c. Transfer the computed liquidated damages amount from column I, Construction, to Column G, Carrying Charges and Financing, on Form HUD-92451and:
      (1) Allocate the full amount to interest, initially.
      (2) Funds may be used for MIP, taxes, or insurance payments, if requested, after the funds for these line items and nonprofit developer's fee, if applicable and working capital escrow are exhausted. However, funds transferred from the construction account may be used to cover only the cost of those items attributable to the period in paragraph 1 above, specified in the construction contract and the assumed completion date.
2. Notify the borrower, contractor, HUD and the surety, if any, by certified mail of the amount and the reason for the transfer.
3. Require written acknowledgment from HUD and surety, if any, before transferring funds.
4. The amount of transferred funds must be reflected on subsequent Forms HUD-92448 as a decrease to item 7, Sum of Cost Breakdown Items Plus Inventories of Materials.
5. After review of the cost certification documents, if the full amount of transferred funds was not needed to cover the cost of interest, MIP, taxes, and insurance attributable to the period identified, the balance will be transferred back to the construction account.

6. In processing Form HUD-92448, before releasing the general contractor's holdback, make adjustment for the lesser of actual or liquidated damages determined in the cost certification review.
7. This procedure should be used only if, in consultation with the Hub Director, it is determined that the problems causing the delay will be remedied within the near future.

12.8 Construction Change Orders – General HUD Duties

A. General instructions. Construction contract changes to the scope of contract work, contract price or contract time must be requested by the mortgagor through the Lender on Form HUD-92437, Request for Construction Changes and must be signed by the mortgagor's Architect, the mortgagor, the general contractor and the Lender. HUD must approve the change order.

1. HUD review and approval. Each HUD discipline as appropriate, including Architecture, Cost, Appraisal, Mortgage Credit and the HUD inspector must review and make a recommendation to the HUD CM.
2. Change orders will be approved only when they are necessary, are for betterment or an equivalent. The following information should appear on the face of the change order:
   a. Classification (necessity, etc.);
   b. Qualification for payment from the contingency reserve and from the developer's fee for nonprofit borrowers; and
   c. Whether the change order results from error, omission or negligence on the part of the Architect, contractor or mortgagor.
3. Change orders submitted after the final HUD Representative's Trip Report will not be approved, except where:
   a. The change order pertains to "Items of Delayed Completion," or
   b. Written approval is given by the Hub Director.
4. Surety approval must be secured in writing before approving any change or aggregate of changes that increase the contract price by 10% or more. Surety consent is not required where the project's assurance of completion is by a cash escrow or letter of credit.
5. Working capital construction contingency. The working capital escrow requirement for new construction transactions is 4% of the mortgage amount, half of which (or 2%) is a construction contingency to be used to fund "necessary" approved change orders, construction cost overruns and other cost overruns. The 2% construction contingency portion of the escrow will be refunded to the developer at Final Endorsement, if not used. Change orders funded from the contingency portion of the working capital escrow will not be considered as the basis for a request for an increased mortgage amount.

B. Other change order policies.

1. Changes must be accurately reported and accounted for pursuant to U.S. Criminal Code, Section 1010, Title 18, U.S.C.
2. Procedures for changes outlined here are not to be used to alter the intent of the contract documents or to lower the quality or value of a project.
3. HUD does not initiate any change but may require it as a condition of approval in connection with a change proposed by the Architect, mortgagor or contractor.
4. All changes must be approved in writing by the Lender and HUD before they are made.
5. Any change that is made without formal approval, even though tentatively agreed to as technically acceptable, must be recorded by the HUD inspector as a noncompliance until the Form HUD-92437, Request for Construction Changes - Project Mortgages, is approved, and it will also affect payment of advances.

C. Change order classification.

1. Necessary changes (which the Construction manager or architectural designee must document) are those that arise from:
   a. Latent conditions that differ from conditions defined by the construction documents;
   b. Changes in the applicable state or local codes, ordinances, etc. after:
      (1) Initial closing for insured advances; or
      (2) Firm Commitment for insurance upon completion.
   c. The Architect's errors or omissions.
   d. Damage to completed construction.
2. Betterment changes are those that are economically justified. They must either:
   a. Increase net income;
   b. Reduce long-term project maintenance and/or operating expenses; or
   c. Otherwise enhance the mortgage security.
3. Equivalent changes are those proposed because:
   a. A specified item is not readily available and the substitution provides equivalent or better utility and performance, or
   b. The proposed substitution reduces the contract price but provides equivalent or better utility and performance.

D. Additive change orders. The Lender must not give any explicit or implied assurance to the mortgagor or the contractor that an increase in the insured mortgage amount will be granted when construction changes are approved.

1. Lender must require the mortgagor, except for "necessary" change orders on substantial rehabilitation projects, to escrow funds with the Lender for any additive change order where HUD first estimates that the aggregated change orders equal or exceed a $5,000 increase in the

construction contract price, and for all subsequent additive change orders. Nonprofit mortgagors may use the Developer's fee to fund additive change orders.

a. Excess mortgage proceeds, if available, may be used to fund the escrow for "necessary" and "betterment" change orders. However, any excess mortgage proceeds used to fund the escrow for contractor estimated costs in excess of HUD estimated costs, or HUD estimated costs in excess of contractor estimated costs, may not be disbursed until final closing.

b. The Lender may accept a third party letter of credit instead of a cash deposit, subject to the Lender agreeing to provide the cash equivalent, where the letter of credit is not immediately honored.

c. The Lender may recognize the cost of third party paid change orders at cost certification, where there are available mortgage savings.

2. On substantial rehabilitation projects, the Lender must approve payment from the established contingency reserve in an amount not to exceed the HUD cost estimate for "necessary" additive change orders or betterments.

a. The Lender must require an escrow for any amount that the contractor's cost estimate exceeds the HUD estimate.

b. The Lender may authorize the use of excess mortgage proceeds, if available, to satisfy the escrow requirement, subject to the disbursement limitations in paragraph 12.8.D.1.a above.

3. The Lender must approve the following forms for mortgagor's application of funds for completed additive change orders:

a. Form HUD-92464M, Request for Approval of Advance of Escrow Funds, where an escrow is used, which must be submitted to HUD for approval.

b. Form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds, where a rehabilitation project's contingency funds or a nonprofit's Developer's fee or excess mortgage proceeds are to be used.

E. Deductive change orders. Where the HUD estimated decrease in contract price for any aggregation of change orders:

1. Remains less than 2-1/2% of the contract price, the Lender must reduce the Contractor's "Final" Requisition, Form HUD-92448, by the appropriate amount.

2. Equals or exceeds 2-1/2% of the contract price and for all subsequent deductive change orders regardless of the amount, the Lender must:

a. Reflect the decrease in the Contractor's Requisition, Form HUD-92448, item 8.

b. Reduce the original mortgage amount at cost certification, where required.

F. Changes that adversely affect property income are a basis for change order rejection, except where it is a necessary change order and the situation is unavoidable.

G. Extension of contract time.

1. The Lender may approve an extension only where:

a. The delay is beyond the contractor's control (e.g. strikes, differing site conditions, bad weather exceeding the average for the season, etc.) and it is documented or associated with an approved change order,

b. The extension request is submitted within the limit provided by the contract and the general conditions for delays beyond the contractor's control, and submitted concurrently with any requested changes in the work, and

c. The request is accompanied by a Surety's written consent. There is no consent requirement where the project's assurance of completion is by a cash escrow or letter of credit.

2. The Lender may require funding for the increased cost for overhead, interest, taxes, insurance, MIP and contractor's general requirements by use of a cash escrow, excess mortgage proceeds, or nonprofit's developer's fee, if applicable, or from contingency reserve.

3. HUD may enforce liquidated damages in accordance with the contract.

4. Required documentation. Within 21 days of the date a construction delay occurs, the contractor must document it with the Architect and include:

a. Date of occurrence and number of calendar days it covered;

b. Effect on construction progress;

c. Cause of the delay. If the cause is of a continuing nature, submit the extension request when the cause ceases, but still record the initial date of occurrence and its effects on construction; and

d. The extension request must include the written consent of the Surety and conform to AIA Document A201, Article 8.3.

H. Changes to items of delayed completion are the only construction contract changes that the HUD Representative may approve after project completion. All others require the Hub Director's consent.

I. Emergency changes.

The only time a change can be made without prior written approval of the Lender and HUD is in emergencies that:

a. Endanger life or property; or

b. Halt construction.

However, even then, the Architect must notify the Lender and HUD and as soon as possible, submit a Form HUD-92437.

J. Insurance Upon Completion: Construction Contract Changes, Form HUD-92437, are to be processed in the same way as Insurance of Advance cases, except as modified below:

1. An escrow is not required for additive change orders. The borrower:

a. Must be able to provide the additional funds required, and,

b. Must not have any outstanding obligation in connection with construction other than the insured mortgage at the time the mortgage is presented to HUD for insurance upon completion.

2. Surety approval is not required for the approval of additive change orders regardless of the percentage of contract increase.

K. Changes to offsite construction must be requested by letter or other acceptable format with the information required by Form HUD-92437 used as a general guide, although the actual form must not be used.

L. Other changes. Changes necessitated by error, omission or negligence of the Architect, owner, or contractor must be recorded by the HUD architectural staff or inspector, on Form HUD-92437, including.

1. The reason for the determination; and
2. Confirmation that the cost of the changes must not be included in the mortgage amount.

12.9 Change Orders – Inspection Instructions

A. General procedure.

NOTE: For projects involving insurance upon completion, references here to "contract requirements" or "contract documents" include the conditions and provisions of the commitment if there is no construction contract.

1. Any contemplated changes are first discussed among the Architect, contractor, owner, and HUD inspector.
2. HUD inspector will make a preliminary determination of technical acceptability before the change is submitted for approval to the Lender and the HUD Office. (This neither commits HUD to the change, nor relieves the Architect or the contractor of having to submit Form HUD-92437.)
3. All onsite changes to construction documents and requests for time extensions must be submitted for approval on Form HUD-92437, Request for Construction Changes - Project Mortgages.
   a. Required attachments for physical changes are:
      (1) Appropriate modifications to the contract drawings and specifications;
      (2) Architect's statement that the change:
         (a) Conforms to the original intent of the contract drawings and specifications;
         (b) Is necessary to overcome an impediment to construction, or is an addition desired by the owner.
      (3) Backup documentation for the amount requested consisting of itemized quantities and costs.
   b. The form must be signed by the:

(1) Borrower,

(2) Contractor,

(3) Architect (if an Owner-Architect Agreement is in effect), and

(4) Authorized official for the Lender.

4. All offsite changes to construction documents and requests for time extensions must be:
   a. Requested in a letter or other format acceptable to the Hub/PC, but not on Form HUD-92437.
   b. Documented and processed the same as on-site changes.
5. HUD will promptly review all requests submitted so delays will not affect construction or contractor requisitions
   a. Processing should normally take no more than 5 workdays and is directed by the CM.
   b. All construction change requests must be reviewed, signed, and dated by the CM.
6. Voiding changes. If an approved change is not made, it must be nullified by a Form HUD-92437 restoring the drawings and specifications to the status prior to the change request or to a status acceptable to HUD.
7. Unapproved changes. When there are unapproved changes in the construction, the HUD inspector must modify the amount of the contractor's requisition to cover:
   a. The non-compliance (any change that has not formally been approved on Form HUD-92437), and
   b. Construction removal that may be required if the unapproved change does not receive approval.

12.10 Change Orders – HUD Architectural and Cost Instructions

A. Architectural. The HUD construction analyst will review all requested changes for technical acceptability.

B. Cost.
   1. Construction changes:
      a. The HUD cost estimator will produce a cost estimate for each construction change request submitted by the mortgagor by applying current data to accepted or amended change order quantities; include amounts for general requirements and builder's overhead and profit using the percentage of each from Section G of Form HUD-92264 that was approved at Firm review.
      b. Compare the estimate with the mortgagor's estimate and, if reasonable, use the mortgagor's figure. Otherwise use the HUD estimate.
      c. Complete the cost entries on Form HUD-92437 and forward the completed form to the HUD mortgage credit examiner and/or the appraiser, if applicable.

2. Approved time extensions:
   a. Calculate the additional general requirements cost due to the extension of time.
      (1) Divide the cost of general requirements from the contractor's approved Form HUD-2328 by the number of months estimated for construction from Section G of Form HUD-92264 approved at Firm commitment. Sixty-five percent of this amount is the estimate per month of additional general requirements.
      (2) Use one quarter of the monthly estimate per week.
      (3) There is no cost effect for extensions of time for less than one week.
   b. Complete the cost entries on Form HUD-92437 and forward the completed form to the HUD appraiser and mortgage credit examiner.

12.11 Change Orders – HUD Appraisal and Mortgage Credit Instructions

A. Appraisal.
   1. The HUD appraisal staff must review all requested changes that may affect marketability, value, income, or maintenance or operating cost; and identify and explain any estimated increase or decrease in net project income on the reverse of Form HUD-92437.
   2. The appraiser must forward a Trial Form HUD-92264 and Trial Form HUD-92264-A reflecting the new data for Mortgage Credit re-determination of the maximum insurable mortgage.

B. Mortgage credit.
   1. Processing.
      a. If the borrower's or contractor's estimate for the change order exceeds HUD's estimate, the difference must be escrowed with the Lender. Excess mortgage proceeds, if available, may be used to satisfy this requirement. Conversely, that portion of HUD's estimate which exceeds the borrower's or contractor's estimate must be restricted and held until final endorsement to ensure funds to complete the project.
      b. Process the cost and appraisal findings and show the cumulative effect on cost of all approved change items.
      c. Use Sections 12.8.D and 12.8.E for additive and deductive change orders.
      d. Recalculate the maximum insurable mortgage when any approved construction change or changes adversely affect net income, e.g., a change that causes an increase in project operating costs or a reduction in project income.

(1) Appraisal completes a Trial Form HUD-92264 with an updated income and expense analysis.

(2) Re-determine the maximum insurable mortgage.

(3) If the re-determined mortgage is lower than the original mortgage amount, as a condition of approval of the change order, indicate in item 3b of Form HUD-92437 that subsequent Contractor's Requisitions, Form HUD-92448, must be reduced by the greater of:

(a) The difference in mortgage amounts;

(b) The net increase in costs resulting from acceptable construction changes.

e. Extensions of time.

(1) Architectural and cost technicians are responsible for determining whether the delay was beyond the contractor's control and, if so, the length of the approved time extension.

(2) Calculate the cost increase due to the extension:

(a) Compute daily rate for interest, taxes and insurance by using estimates in Section G of Form HUD-92264 and multiply these rates by the approved time extension.

(b) An additional year of MIP will be required if the approved time extend, when added to the estimated construction term plus the 2 months included in Section G of Form HUD-92264; plus previously approved time extensions.

(c) Add the additional general requirements, if any, noted by the Cost branch on the change order request.

NOTE: Only Item (c) above amends the construction contract price on Form HUD-92437.

(3) Determine the source of funds for any increase due to the extension, i.e., cash, excess mortgage proceeds or nonprofit's developer fee, or contingency reserve funds.

(4) Requests for release of excess mortgage proceeds or contingency reserve funds set aside to fund time extensions are submitted on Form HUD-92403.

(5) Releases from a cash deposit are made using Form HUD-92464.

(6) These funds may be released only after the account for the soft cost item(s) being requested has been exhausted on Form HUD-92451, Financial Record of Mortgage Loan Transaction.

2. Requests for disbursement of contingency reserve funds, working capital construction contingency funds and nonprofit's developer fee for completed change order items are made on Form HUD-92403. All requests:

a. Must be accompanied by a certification by the borrower's supervisory Architect and the HUD Inspector that all the work covered by the change order has been acceptably completed in accordance with contract documents.

b. Must include the borrower/borrower's certification relative to payment to the contractor contained on Form HUD-92464M, Request for Approval of Advance of Escrow Funds.

c. Must include the criminal certification contained on Form HUD-92464M for certifications made in paragraphs a and b above.

d. Are subject to a 10 % holdback.

3. Change orders funded from excess mortgage proceeds. Excess mortgage proceeds may be used to fund either necessary or betterment change orders.

   a. These funds may be used to fund HUD's estimate of increased costs as well as any portion of the contractor's estimate which exceeds the HUD estimate. The portion which exceeds HUD's estimate must be restricted until final endorsement.

   b. Funds are released in the same manner as contingency reserve funds.

4. Releasing Cash Deposit. The borrower must submit, through the Lender, Form HUD-92464M when construction covered by a cash deposit is complete and acceptable to HUD.

   a. The borrower's supervisory Architect and the HUD inspector must certify on Form HUD-92464M that all work and materials covered by the change order are satisfactory and consistent with contract drawings.

   b. If construction costs were paid in full with other than the cash escrow or excess mortgage proceeds before submitting the disbursement request to HUD for approval, the borrower must submit a receipt of payment signed by the general contractor.

   c. If construction costs will be paid after HUD's approval for the release of the funds deposited for the construction change, before the next Form HUD-92403 is submitted, the borrower must submit a receipt of payment signed by the general contractor.

5. Change Order Summary Sheet showing cumulative cost of all executed change orders should contain, at least:

   a. The date the change order was signed by the borrower;

   b. The date HUD received the change order;

   c. The date the Mortgage Credit branch processed the change order;

   d. The borrower's or contractor's estimate of cost for the change order;

   e. HUD's estimate of cost for the change order;

   f. The amount of change orders to be funded from contingency reserve, working capital construction contingency, nonprofit's developer fee, or excess mortgage proceeds;

   g. The required cash escrow deposit, if any;

   h. The HUD percentage of cost increase or decrease.

12.12 Labor and Fair Housing and Equal Opportunity (FHEO)

A. Wages

1. Payrolls. Contractor payrolls are submitted directly to the HUD Labor Relations staff a minimum of once a month.
2. On-site interviews. The HUD Construction Manager forwards all original copies of Form HUD-11, Record of Employee Interview, which are submitted by the HUD inspector to the HUD Labor Relations Staff.

B. Labor violations. Advise the Labor Relations Staff of continuing minor infractions that cannot be resolved or of any identified or suspected major violations.

C. FHEO noncompliance. Advise the local HUD Director of FHEO of continuing minor noncompliance that cannot be resolved or of any identified or suspected major noncompliance.

12.13 Surveys

Surveys must be by a licensed surveyor and show the exact location of on-site improvements, including utility lines and easements.

A. The contractor must give the owner and HUD surveys:

1. At any time the owner or HUD requires, and
2. When construction is complete (“as-built” survey).

B. The inspector, when uncertain of the location of construction or stored materials in relation to property lines or easements, may ask the Architect to require a survey with the next contractor's requisition.

C. If encroachments are found, the inspector must notify the HUD Construction Manager by memorandum explaining the conditions. (Encroachments may jeopardize the entire property as security for an insured mortgage.)

12.14 Permission to Occupy

Permission to Occupy Form HUD-92485 must be executed by HUD before the borrower permits occupancy of any dwelling unit.

A. Physical completion. The work, or portion thereof for which Permission to Occupy is approved, must be sufficiently complete in accordance with the contract documents so the mortgagor can occupy or utilize the identified portion of the work for its intended use.

1. Support facilities (utilities, disability access, vehicular access and parking, fire life-safety equipment, etc.) must be in place.
2. The acceptability of each unit and facility for which Permission to Occupy is requested must be confirmed:
   a. Property must be inspected and Form HUD-92485 signed by the borrower, supervisory Architect, contractor, and HUD Representative.
   b. Minor items that do not preclude occupancy are permitted but must be listed as an attachment to Form HUD-92485.
   a. The contractor is fully responsible for any incomplete or improperly performed contract work whether or not listed.

B. Signatures, Approval and Permission:

1. Form HUD-92485 must be signed by the borrower, supervisory Architect, contractor and HUD representative.

2. Approval: The Construction Coordinator or a designated MAP staff person in the Program Center signs as Chief, Architecture and Engineering Section. The MAP Team Leader signs as Chief Underwriter.

3. Permission to Occupy: The Hub Director and MAP Coordinator will designate an FHA Authorized Agent in the Hub or PC to sign the Permission to Occupy.

C. Submission Documents. The Lender must sign Form HUD-92485 agreeing with the request and stating that insurance risks have been covered for the project. The borrower must include the following documents with the completed Form HUD-92485:

1. A Certificate of Occupancy or equivalent permit from the governing municipal authority for all units and facilities listed on the Permission to Occupy; and any other required permits or authorizations;
2. A certificate of property insurance from the borrower's insurance company.

D. Partial Occupancy Approval.

1. Favorably consider partial occupancy of units as they become available, where vandalism could be minimized, needed project income is provided, an earlier rent-up date could be achieved, utility costs for occupied units can be metered separately from contractor’s utilities, etc.
2. Approve a series of Permissions to Occupy as units or facilities become available, e.g. individual buildings on multi-building projects, or individual floors or wings on larger buildings.

3. Approve a single Permission to Occupy for all units where dictated by management considerations, e.g. very small projects.

12.15 Escrowed Funds, Letters of Credit, Deposits, Holdbacks and Related Matters

A. Borrower's Application for Escrowed Funds, for HUD approval.

Form HUD-92464M, Request for Approval of Advance of Escrow Funds, must be used where the escrow is to ensure completion of offsite improvements, additive change orders, non-critical repairs (under the Section 223(f) program), or borrower's unpaid construction items at final endorsement.

1. The borrower must initiate and forward Form HUD-92464M to the Lender for its review before submitting the disbursement request to HUD for approval.
2. Require the HUD inspector to reflect the percentage of acceptably completed escrow work on the HUD Representative's Trip Report, Form HUD-95379, and forward a copy after review to the Lender for use in reviewing Form HUD-92464M.
3. Do not authorize advances in excess of the documented percentage completed, less previous payments and a 10% retainage, until work is 50% complete, after which reduce the retainage to 5%.
4. Where excess mortgage proceeds are used to fund an escrow for completion of offsite improvements, additive change orders or mortgagor's unpaid construction items, return the original copy of Form HUD-92464M to the depositor and retain one copy.

B. Release of letters of credit. In the event of a claim:

1. Assignment. HUD will not accept an assignment of the letter of credit to HUD from the Lender.
2. Un-drawn Balance. HUD will treat any un-drawn balance from a letter of credit or escrow agreement as cash held by the Lender.
3. Cash equivalent. The Lender must provide cash equal to the un-drawn balance, if demand on a letter of credit is not met.

C. Working Capital Deposit must be established with the Lender at initial closing and may be funded by cash, or a letter of credit or excess mortgage proceeds, if any.

1. Purpose. The deposit is used to:
   a. Defray the cost of initial marketing and rent-up including: sales and advertising, model furnishing, and equipment and supplies essential to initial rent-up, etc.
   b. Cover project expenses during the first operating year that project income is not expected to cover, including: real estate taxes, permanent property insurance premiums, mortgage insurance premium, ground rents and assessments.

c. Cover shortfalls in interest, taxes, property insurance premiums, mortgage insurance premiums, ground rents and assessments during construction after funds available under the Building Loan Agreement are exhausted.

d. The new construction contingency portion of the escrow will be used for change orders and cost overruns.

2. Control and Release of Escrow. The Lender controls disbursements from the escrow, except where the borrower certifies at firm commitment that any balance of the escrow will be applied to the reserve for replacements or additional betterments on a tax credit project. In reviewing a mortgagor's request for release of part of the escrow, the following must be considered:

   a. Borrower's request for the release of such escrow funds must be by letter to the Lender, rather than on Form HUD-92403.

   b. None of the escrow can be used to defray any of the hard costs of construction applicable to the Total for All Improvements, Section G of Form HUD-92264, Rental Housing Project Income Analysis and Appraisal (or other Firm Stage underwriting form applicable to the Section of Act the project is to be insured under).

   c. Avoid premature disbursements and unnecessary expenditures.

   d. As portions of a project are ready for occupancy, a partial disbursement may be permitted for reasonable opening expenses: however, it must be determined that the escrow is not exhausted before the entire project is complete.

   e. The Field Office may direct that the deposit be used to cover any shortfall in interest, taxes, property insurance mortgage insurance premiums, ground rent and assessments.

   f. Fully document all expenditures from the escrow.

3. Final Release of Escrow.

   a. The Lender may release any unused balance in the working capital escrow, subject to HUD approval, to the mortgagor one year after Final Endorsement where the project is not in default and when the operations of the project have demonstrated to the Hub/PC's satisfaction that the project has achieved 6 consecutive months of break-even occupancy. Break-even occupancy is defined as 1.0 debt service coverage, based on all sources of project income including ancillary income

   b. The Lender must hold this escrow until any project financial problems are resolved (e.g., has not reached sustaining occupancy, has poor liquidity or high payables, is operating at a deficit or is near default).

   c. If the mortgage is in default, the Lender must apply any balance of the working capital escrow to cure a default, where a default occurs before its release.

   d. The working capital new construction contingency will be refunded to the borrower at final endorsement, if not used.

D. Amount of contractor's retainage and release. The retainage provides an incentive for the general contractor and mortgagor to promptly complete the project, submit cost certification and reach final closing.

1. Amount of retainage. The Building Loan Agreement allows for the possibility of a reduced holdback amount as set forth in a Retainage Reduction Rider when the project reaches 50% completion The construction contract also provides for a 10% holdback from the contractor's monthly payments for acceptably completed work, acceptably stored materials, and where applicable, components acceptably stored offsite. The requirements for reduction of the retainage after 50% completion are as follows:

   a. The Contractor has no identity-of-interest with the owner that is greater than a 5% equity interest in the ownership entity,

   b. If applicable, prior written consent from the Surety must be obtained and attached to the request for reduction, and

   c. There can be no questions regarding the contractor's performance concerning the quality of work, compliance with the contract and with any change orders or work in progress. The Hub or PC Director must make the decision to reduce the retainage based on the recommendation of HUD's construction inspector.

   d. Assuming the above conditions are met, the existing standard of 10% retainage will be required only until 50% completion. After 50% completion, the retainage may be reduced to 5% until 75% completion, and then may be reduced to 2.5% retainage until the loan reaches Final Endorsement.

2. Release of retainage for identity of interest contractors. Except as provided in paragraphs 4 and 5 below, the retainage may not be released, in whole or in part, until Final Endorsement for a contractor with an identity of interest.

3. Release of retainage for non-identity of interest contractor. The contractor's retainage, or the remaining balance in the retainage, may be released at the next to last advance, when requisitioned on Form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds, and subject to compliance with the following:

   a. Contractor's cost certification, where required, has been reviewed and necessary adjustments made to Form HUD-92451, Financial Record and Mortgage Loan Transaction;

   b. Contractor has disclosed its final obligations on Form HUD-92023M, Request for Final Endorsement of the Credit Instrument;

   c. All work under the construction contract has been inspected and approved by the controlling jurisdictions and/or authorities;

   d. Certificates of occupancy or other required approvals for the dwelling units and non-dwelling facilities, where applicable, have been issued by governmental authorities having jurisdiction. (Separate buildings for community rooms, rental offices, laundry rooms, etc., commonly require separate certificates of occupancy.);

   e. Permission To Occupy, Form HUD-92485 has been issued by HUD for all units;

f. All Davis-Bacon payroll requirements have been satisfied;

g. Surveyor's Certificate, Form HUD-92457M, and survey showing the location of all improvements, utility easements and site utility distribution lines have been submitted to HUD, and

h. Retain, where applicable, an adequate amount to cover the following:

(1) Items of delayed completion in an amount equal to 150% of the HUD representative's cost estimate for completion,

(2) Any owed or contested amounts indicated by mechanics, subcontractor, supplier, or equipment lessor liens, etc.

(3) The lesser of the liquidated damages or actual damages computed at cost certification, and

(4) The net effect of any negative change orders.

4. Early partial release of retainage.

a. After 90% contract completion, the Hub Director may release part of the contractor's holdback and suspend further withholding of holdback from payments due, where:

(1) The contractor has no identity of interest or the contractor's only identity of interest in the project ownership is less than 5%;

(2) The contractor, mortgagor and mortgagee request the early release of the holdback and attach the request to Form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds; and

(3) Prior written consent from the surety, if any, for the early release of holdback is provided with the request.

b. The Hub Director determines that:

(1) The contractor's general performance warrants partial release of the holdback without conditions, or

(2) A partial release of the holdback is appropriate with conditions, e.g., measures to assure immediate distributions to subcontractors or others, would be in the mutual interest of all participants, and

c. The un-disbursed holdback amount must equal or exceed 5% of the contract amount.

5. Projects in difficulty. Release of part of the contractor's holdback before 90% contract completion may be granted only to prevent a default of the construction loan and only if it would solve the project's problems and enable it to reach construction completion.

a. The contractor's performance must be considered, including:

(1) The completed work must be satisfactory,

(2) The percentage of completed contract work must be sufficient to ensure project completion within the specified contract time, and

(3) The holdback may not be released if there are serious, unresolved questions concerning:

(a) Quality of work,

(b) Compliance with the contract, including outstanding change orders, or

(c) Work is progressing behind the contractor's construction schedule, as amended by approved change orders.

b. Written consent for the early release of holdback must be obtained from the surety, if any, the mortgagor and the mortgagee.

E. Initial Operating Deficit Deposit must be established with the Lender at initial closing and may be funded by cash or a letter of creditor excess mortgage proceeds, if any.

1. The operating deficit escrow provides funding for operating expenses and debt service when net income is not available during the initial lease up period. This escrow is not mortgageable and the unused portion must be returned to the Borrower.
2. Release of the Initial Operating Deficit Escrow. HUD will consider Lender's request using Form HUD-92476.a-M, Escrow Agreement for Operating Deficit, for all initial operating deficit draws during lease-up. The Lender's request must be accompanied by:
   a. A review and analysis of the monthly accounting reports detailing progress on lease up as compared to the lease up projections used in underwriting, and
   b. An updated calculation of the sufficiency of the escrow. This analysis and calculation is particularly important if the project is experiencing substantial variations from its lease up projections.
   c. Unused amounts will be released upon the Lender's request at the later of 12 months after Final Endorsement or when the project has demonstrated to the HUD field office's satisfaction that the project has achieved 6 consecutive months of break-even occupancy. (Break-even occupancy is defined as 1.0 debt service coverage, based on all sources of project income including ancillary income.) HUD Mortgage Credit staff will consult with Asset Management (AM) staff prior to approval of a release to obtain AM's approve of the release. Hubs/PCs should exercise caution to be certain that monthly results are not erratic or seasonal and that 1.0 or better debt service coverage will be sustainable after release of the escrow funds. For garden apartment projects consisting of separate buildings, each of which is leased up separately, HUD will consider partial releases of the operating deficit escrow as individual buildings achieve 6 consecutive months of break-even occupancy. The Lender is responsible for insuring that escrow funds are released solely for project operating needs.

F. Cash-Out From Land Equity must be held by the Lender at initial closing and is funded by excess

mortgage proceeds, if any.

1. Cash out from the excess value of the land, or, for a substantial rehabilitation project, the "as is" property value, that was contributed to meet the sponsor's equity requirement at initial endorsement, **above** what was required at initial endorsement must be deferred and held by the Lender. The Lender will have discretion as to the form of escrow to use to hold back any cash out from land equity, refer to Appendix 12A paragraph E.
2. The Lender will hold the cash out funds until project operations have demonstrated to the HUD field office's satisfaction that it has achieved 6 consecutive months of break-even occupancy. (Break-even occupancy is defined as 1.0 debt service coverage, based on all sources of project income including ancillary income.) HUD Mortgage Credit staff will consult with AM staff prior to approval of a release to obtain AM's approve of the release. Multifamily Hub/Program Centers should exercise caution to be certain that monthly results are not erratic or seasonal and that 1.0 or better debt service coverage will be sustainable after release of the escrow funds. HUD will approve a request for release of funds on Form HUD-92464M from the Lender. The Lender's file should contain the HUD approval and documentation supporting the release.

12.16 Insurance Upon Completion

A. Basic requirements during construction stage are generally the same as for projects with insured advances. However, because HUD does not insure advances for the construction loan, HUD does not monitor the Lender's disbursements. Additionally, because HUD has no risk exposure until final endorsement, HUD does not become involved in the workout of construction problems. The following are major variations from standard program requirements for insurance upon completion projects.

B. Firm Commitment to Insure Upon Completion, Forms FHA-2453, FHA-2453-MM (for Section 223(f)), must be valid and outstanding until Final Endorsement of the permanent mortgage.

1. No initial closing. The construction stage starts after the issuance of the Firm Commitment.
2. Construction/rehabilitation must start and be completed within the period provided by the Firm Commitment.
3. Extensions. See Chapter 11 for the extension of:
   a. Construction period;
   b. Firm Commitment expiration date, where required to permit project completion and Final Endorsement.

C. Required documents include:

1. Construction contract, Form HUD-92442M. The following must be made a part of the contract:

a. General Conditions, AIA Document A201;
b. Supplementary General Conditions, Form HUD-92554M;
c. Davis-Bacon Wage Rates (supplied by HUD Labor Relations);
d. HUD Amendment to the B108, Owner-Architect Agreement to Identify Identities of Interest Between Owner/Contractor/Subcontractor/Architect;
e. Cost certification criteria from Form HUD-92442M, Article 13, where an identity of interest exists or a "cost plus" form of contract is used.

2. A complete master set of drawings and specifications and two duplicate sets;
3. The Agreement and Certification, Form HUD-93305M, executed by the mortgagor, Lender, and HUD.
4. A title policy or title evidence showing:
   a. Insured property free of all encumbrances other than the mortgage and acceptable reservations of title;
   b. Proof that no unpaid obligations exist except as previously approved by HUD;
   c. Title policy continued to date of credit instrument endorsement.
5. Survey and Surveyor's Certificate, Form HUD-92457A-M;
6. Contractor's Requisition Project Mortgages, Form HUD-92448. The Contractor's Prevailing Wage Certificate must be submitted at the time the mortgage is presented to HUD for insurance.
7. Assurance of funds to meet operating deficit. Completed Forms to assure funds are available to carry the project to a sustaining occupancy after final closing:
   a. HUD-92476M, Agreement of Sponsor to Furnish Additional Funds,
   b. HUD-92476a-M, Escrow Agreement for Operating Deficit, and
   c. HUD-92477M, Bond Guaranteeing Sponsor's Performance.
8. Assurance of completion: Not applicable to insurance upon completion projects.
9. Warrantee against latent defects is required in accordance with Section 12.16.S.

D. The pre-construction conference must precede the initial start of construction, see Section 12.2.

E. Construction monitoring and reporting must be done in accordance with Section 12.3.

F. Labor and FHEO liaison, see Section 12.12.

G. Contractor's monthly requisitions are not applicable to projects insured upon completion.

H. Offsite construction:
   1. Monitoring is recorded by the HUD inspector on Form HUD-95379.

2. Advance of funds monitoring is not applicable to projects insured upon completion.

I. Construction contract changes and Architect's supplemental instructions (see Sections 12.8 to 12.11 and 12.4.D). Construction changes are processed in the same manner as insurance of advances, except as modified below:

1. An escrow is not required for additive change orders, because HUD has no risk exposure until final closing. The mortgagor must be able to provide the additional funds required and must not have any outstanding obligation in connection with construction other than the insured mortgage at the time the mortgage is presented for insurance.
2. Surety approval is not required for the approval of additive change orders regardless of the percentage of contract increase.

J. Permission to Occupy applies as in Section 12.14.

K. Final HUD representative's Trip Report falls under HUD procedures.

L. Guarantee period falls under HUD procedures.

M. Working capital deposit and operating deficit escrows are not usually required for Insurance Upon Completion projects. However, to mitigate any risk, projects that apply for Insurance Upon Completion must fully meet the operating deficit escrow and the working capital requirements contained in Section 8.13, except for the extra 2% new construction contingency portion of the working capital escrow which is not required. See Sections 12.15.C and 12.15.E for releasing escrowed funds.

N. Property insurance schedule and requirements. When onsite construction is 80% complete (before Final Endorsement of the mortgage), the Lender must prepare:

1. Property Insurance Schedule, Form HUD-92329, that:
   a. Correctly shows the insurable value of the completed structures;
   b. Reflects any changes in cost occurring after issuance of firm commitment.
2. Property Insurance Requirements, Form HUD-92447.

O. MIP is not charged until the project reaches final closing.

P. Cost certification (see Chapter 13).

Q. Closing must occur within the period provided in the commitment.

R. Extension of Firm Commitment instructions are in Chapter 11.

S. Builder's warranty. The general contractor must enter into a latent defect agreement with HUD and provide one of the following at Final Endorsement to assure correction of any latent defects:

1. Cash escrow deposit of 2.5% of the principal amount of the mortgage, to be retained in escrow by the Lender for a period of 15 months, or
2. An irrevocable, unconditional letter of credit issued to Lender by a banking institution, or.
3. Surety bond in the amount of 10% of the cost of construction or substantial rehabilitation. The bond must be in effect for 2 years after substantial project completion. The bond must be on Form HUD-3259, Surety Bond Against Defects Due to Defective Materials and/or Workmanship.

12.17 Completion of Repairs Pursuant to Section 223(f)

A. Required Repairs are to be documented by the Lender with a list that categorizes repairs as critical repairs or non-critical repairs. (See Chapter 5, Section 5.26 and Appendix 5H)..

1. Critical repairs must be completed before closing. Critical repairs are any individual or combination of repairs required to correct conditions that:
   a. Endanger the safety or well-being of residents, visitors or passers-by;
   b. Endanger the physical security of the property;
   c. Adversely affect project or unit(s) ingress or egress; or
   d. Prevent the project from reaching sustaining occupancy.
2. Non-critical Repairs consist of all repairs other than Critical Repairs. Non-critical Repairs may, at the request of the mortgagor, be completed after closing.
3. Completion of repairs.
   a. Before closing. Critical repairs must be completed before closing. A site visit(s) and report(s) by a HUD representative is required to confirm satisfactory completion of required repairs before closing.
   b. After closing. Only non-critical repairs may be completed after closing. The following schedules are required:
      (1) Schedule of Values for payment of completed repairs;
      (2) Progress Schedule. All repairs must be completed within 12 months of loan closing;
      (3) Schedule of Delayed or Interrupted Occupancy or Income, must list:
         (a) All facilities for which occupancy or income will be delayed or interrupted by repairs delayed until after closing;
         (b) Period of delayed or interrupted occupancy or income;

(c) Projected completion date.

(4) Release of Cash/ Equity from Loan Proceeds. For projects with cash out proceeds and incomplete non-critical repairs, an escrow equal to 50% of the balance of cash out proceeds (after funding transaction costs and the assurance of completion requirement), must be established at Initial/Final Endorsement, on Form HUD-92476.1M, Escrow Agreement for Non-Critical, Deferred Repairs. These funds must be held by the Lender until all required non-critical repairs are complete. The borrower can request release of these funds after completion of the repairs and with written approval of HUD.

4. Payment for Repairs.
   a. Repairs completed before closing: No mortgage proceeds may be advanced.
   b. Repairs completed after closing:

      (1) A completion repair escrow account must be established and held by Lender in an amount equal to 120% of the estimated repair costs (see Section 5.26.D.2).

      (2) The Schedule of Values for completed repairs will be provided to the HUD inspector, who will recommend progress payments from this Schedule as a part of the Trip Report, Form HUD-95379.

B. Inspection of completed repairs is performed by the HUD inspector.

1. Inspection Reports are filed on Form HUD-95379, HUD Representative's Trip Report, for each monitoring visit. The following are included in the Trip Report:
   a. Non-compliance with provisions of the commitment or closing, e.g. work write-up, drawings, specifications, etc., including changes made to the work without prior approval;
   b. Adverse conditions e.g. slow work completion, destruction of work, new municipal requirements, disputes, etc.
   c. Availability for use of facilities listed on the schedule of delayed or interrupted occupancy.
   d. Municipal authorizations. Permissions to occupy use permits, etc. Where applicable, these must be issued before closing, unless related to work delayed until after closing;
   e. Items of delayed completion. The HUD inspector must include:

      (1) A detailed list of any exterior work;

      (2) Recommended escrow amount; and

      (3) Recommended completion date (not later than 12 months after closing);
2. Assignment documents. The HUD inspector should assemble the following documents to monitor repairs and recommend payments:
   a. Firm Commitment;

b. Escrow agreement (where closing has occurred);
c. Survey, surveyor's report and legal description;
d. List of required repairs (work write-up);
e. Drawings and specifications (where required);
f. Schedule of Values (required only for projects with repairs delayed after closing);
g. Progress schedule (required only for projects with repairs delayed after closing);
h. Schedule of delayed or interrupted occupancy or income (required only for projects with repairs delayed after closing); and
i. Agreement and Certification.

C. Repair completion. All work must be acceptably completed before the loan closing, except for the following:

1. Minor exterior work, which cannot be completed because of weather conditions, may be completed after closing, on projects for which prior provisions were not made for completion of non-critical work after closing; include the amount (s) to be escrowed.
2. Non-critical repairs may be completed after closing when provided in the commitment and when a completion escrow is established at closing, except that:
   a. All critical repairs must be completed before closing, and
   b. An additional deposit must be made to the operating deficit account for delayed repairs which will delay or interrupt occupancy or income for any period. The amount of the additional deposit will be determined by HUD.
3. Repair monitoring. All work must be monitored and be acceptable to the Lender and HUD whether it is performed before or after closing.

D. Final report must be made upon completion of all work. The final report must show that:

1. All work is acceptably completed in accordance with the firm commitment and/or closing escrow, as applicable, and approved changes;
2. Offsite work is completed or that the municipality has given written assurance for its completion;
3. Utilities are connected;
4. Permanent ingress and egress facilities are provided, and
5. Applicable municipal inspections, approvals, etc., have been issued.

E. Changes in the work, including associated cost changes, must be submitted by letter or other acceptable format. Form HUD-92437 may be used as a general guide, but the actual form must not be used.

1. Borrower, HUD and Lender must sign all changes;
2. Contractor and borrower's Architect, if employed, must sign all changes.

F. Guarantee inspections. Where the owner uses a contractor, rather than its own staff, to carry out repairs, guarantee inspections will be scheduled to discover and require correction of latent defects within 1 year of the date of substantial completion of all repairs. See Sections 12.6.C and 12.16.C.

G. Projects in difficulty. Projects in difficulty mean any project having physical, financial, or management problems that could be an indication that a default is imminent. For further explanation see Management Agent Handbook 4381.5 REV-2 Exhibit 6-1.

1. If the borrower has not completed all deferred repairs by the end of the repair period (including any approved extensions), the HUD Inspector will document all such non-completed repairs on Form HUD-95379, HUD Representative's Trip Report, and will submit the report to the Lender with a copy to the HUD CM.
2. The Lender will complete the repairs using the escrowed funds. The Lender will submit a work schedule to HUD for the completion of all remaining repairs, and will provide the borrower with a breakdown of these repairs and the cost(s) of completion (including administrative expenses).
3. Funds remaining in the repair escrow account after completion of the repair work by Lender will be returned to the borrower, less reasonable administrative costs incurred by Lender in completing the repairs.

Chapter 13

Cost Certification

13.1 Projects that Must Certify

Cost certification is required for all insured multifamily projects, except for rental projects insured under Section 207/223(f) refinances where the mortgage is 80 percent or less of value.

13.2 Purpose of Certification

The purpose of certification is to establish the borrower's actual costs, including contractor's cost, to establish the "maximum insurable mortgage" for Final Endorsement of the insured mortgage.

13.3 Certifiable Costs

Certifiable costs are those costs that have been paid in cash or will be paid in cash within 45 days of final closing, except for:

A. Land Value which HUD will calculate,

B. General Overhead which is certifiable whether or not it is paid in cash,

C. BSPRA, which is cost certifiable whether or not it is paid in cash, where there is an identity of interest between the borrower and contractor, and

D. Non-profit Developer's Fee, which is cost certifiable whether or not it is paid in cash, less amounts certified to and allowed on other line items.

13.4 Projects with LIHTCs are Exempt from Cost Certification Requirements

The Housing Economic Recovery Act (HERA) of 2008 affected the borrower's obligation to certify "actual cost" under the insurance programs. If it is determined at the time of Firm Commitment issuance that the ratio of loan proceeds to the actual cost of the project is less than 80 percent, the borrower is not required to certify "actual costs" upon completion of project construction, rehabilitation or repair for

mortgage insurance transactions involving tax credits. This exemption will apply to applications involving LIHTC, Historic Tax Credits or New Market Tax Credits. For example, in cost programs such as 221(d)(4) and 220, when the "Maximum Insurable Mortgage" derived utilizing Form HUD-92264-A is less than 80 percent of the Total Estimated Replacement Cost of Project derived under Section G line 74 of Form HUD-92264, the borrower will not be required to certify actual cost to HUD. See an example of this computation under Section 13.4.A, below.

Note the mortgagor and the general contractors do have the option to certify the actual costs according to the guidance in Sections 13.6 through 13.19.

A. This example illustrates the applicability of the cost certification requirements for Section 221(d)(4). When calculating the maximum mortgage amount the lowest controlling criteria must be utilized. Criterion 11 is used in the example since it will often control as the Maximum Insurable Mortgage under LIHTC applications.

   Form HUD-92264-A Criterion 11

   Amount Based on Deduction of Grants, Loans, Tax Credits and Gifts for Mortgageable Items:

   Total Project Replacement Cost (from Section G. Form HUD-92264)…….. $ 13,000,000

   Tax credit equity for Mortgageable Items ……$ 5,000,000

   Maximum Insurable Mortgage Amount ……..$ 8,000,000

   $ 8,000,000 / $13,000,000 = 62%

   In this example, a cost certification is not required for a tax credit project since the ratio of loan proceeds to the firm commitment estimated project replacement cost is less than 80%.

B. Audit Fee

   In cases that are exempt from cost certification, a Cost Certification Audit Fee, Section G line 66, on Form HUD-92264 is not applicable. The borrower and the general contractor may certify to their actual costs. Should they decide to cost certify per HUD's methodology, the audit cost is mortgageable.

C. Substantial Completion Date

   For projects that are exempt from providing a cost certification the HUD office will notify the Lender of the substantial completion date when the project reaches 100% substantial completion, as officially determined by the HUD Inspector's signature on the final HUD Representative's Trip Report, Form HUD-95379.

D. Operating Income Generated During the Construction Period

   The borrower must account for all operating income during construction and ending three months prior to the originally scheduled date of the first principal payment under the mortgage. In cases such as a substantial rehabilitation tax credit project, without significant resident displacement, it is not unusual to have considerable NOI generated during the construction period. This interim

income may be used to pay for mortgageable and non-mortgageable items. Therefore, an Operating (or Income and Expense) Statement must be submitted covering the period from first occupancy (if occupancy occurred during construction) or from the date of substantial completion through the period ending three months prior to the date of the first principal payment of the originally scheduled mortgage date. The borrower may include in the operating statement all soft costs incurred up to 60 days beyond this date, which will establish the cut-off date for the annual financial statement/ operations reporting. The statement must be submitted to HUD at least 30 days prior to the date scheduled for Final Endorsement. If the income and expense statement evidences receipt of NOI during this period, the borrower is able to apply the income according to the following:

1. If the replacement cost mortgage (Criterion 3) is not the controlling mortgage, any NOI generated during construction may be applied to cover shortfalls in mortgageable soft costs, change orders, initial operating deficit and escrows. At Final Endorsement the balance of funds may be distributed to the borrower or deposited to the Reserve for Replacement account or applied toward the amortization of the mortgage principal. For Non-Profit borrowers processing under the 221(d)(3) program the balance of income must be deposited into the project's Reserve for Replacement account.
2. If the replacement cost mortgage (Criterion 3) is controlling, the Mortgage Credit staff will determine if the balance of the net operating income is equal to or greater than 1% of the original mortgage amount and, if it is, will deduct this amount from the certified replacement cost. When the NOI does not meet this 1% threshold, it can be used toward shortfalls as instructed in number 1 above. Any remaining balance must be deposited into the Reserve for Replacement account at Final Endorsement and there is no distribution to the mortgagor. For Non-Profit borrowers processing under the 221(d)(3) program, the balance of income must be deposited into the Reserve for Replacement account.
3. See Section 13.19.C below on the distribution prohibition for a borrower's affiliate or principal.

E. Copy of Final Sources and Uses Statement. The Lender may submit a copy of the final Sources and Uses Statement prepared by the state tax credit allocating agency to assist in the Lender and HUD review of the final amounts of sources, income and uses.

F. Modification to Form HUD-92580 – Determination of Maximum Insurable Mortgage

For those projects that are exempt from providing a cost certification, after substantial completion, the Hub or PC will issue a modified Form HUD-92580, as illustrated below. Strikeouts are illustrated on line items 2 and 10, below:

1. (a) Original Mortgage Amount …… $10,000,000.00

   (b thru e) are not applicable - *Insert N/A or cross through.*
2. ~~Certified Actual Cost~~ – *Strike* certified actual cost and *Insert Replacement Cost From Section G Line 74* ……..$13,000,000
3. Disallowed Cost ……*(Insert N/A)*……..…….....$_N/A_____

4. Recognized Actual Cost of Improvements … (Sec. G Line 74) $13,000,000
5. Land …….……....$_____
6. TOTAL LAND AND IMPROVEMENTS ……..……$13,000,000
7. Statutory Percentage of Total Cost (____ % of item 6) …….....$___N/A___
8. For Substantial Rehabilitation-Property Owned, enter the Lesser of:

   (i) $_____existing Mortgage Indebtedness on (Land and Improvements to be Rehabilitated) or (ii) An Amount Equal To _____% of the Fair Market Value $_____ of Land and Improvements Before (Repair or Rehabilitation) …….$____N/A_____
9. TOTAL Line 7 plus line 8, (if any) ……..$____N/A_____
10. Maximum Insurable Mortgage in Multiples of $100, (Item 1(a)) or Item 6 whichever is the Lesser) ~~(Item 1(e) or Item 9 whichever is the Lesser) if Grants involved see attached Sheet to this form for Reconciliation of Adjustment, if required~~ …….$10,000,000

NOTE: The Mortgage Credit staff should note on this Form that the project is exempt from cost certification due to the *loan proceeds* to actual cost being less than 80%. Insert the actual percentage of the loan to cost _____.

Completion of the reverse side of the Form as follows:

Schedule 1 N/A

Schedule 2 Disallowed Costs: N/A

Schedule 3 Computation of Borrower's Initial Equity Investment

1. Total Land and Improvements (line 6 above) $13,000,000
2. Less: Maximum Insurable Mortgage (line 10 above) $10,000,000
3. Borrower's Initial Equity Investment $ 3,000,000

13.5 Types of Cost Certification

A. Standard or "Long Form" Certification is required, except for projects permitted to use the "simplified" cost certification and for certification of projects insured under Section 207.

B. Simplified Certification is restricted to projects involving 40 units or less of proposed construction or substantial rehabilitation and is used for projects under Section 207/223(f).

C. Section 223(f) Certification is required for all projects insured under Section 207 except the certification is not required for Section 207/223(f) transactions where the insured mortgage is 80% or less of the value.

D. Section 223(f) Supplemental Certification is required for projects identified in paragraph C above, where completion of repairs is permitted after closing

13.6 Entities That Must Cost Certify

A. The Borrower must certify for all projects, except where HUD has determined at the time of issuance of the Firm Commitment that the insured mortgage under: a) Section 221(d)/220 new construction/substantial rehabilitation is 80% or less of cost, or b) Section 207/223(f) refinance is 80% or less of value, **and** the projects are assisted with LIHTC, Historic Tax Credits or New Market Tax Credits.

B. When the Borrower is required to cost certify, the Contractor must also cost certify when:

1. The Contractor has an identity of interest with the mortgagor, whether such identity of interest existed or developed before or after the initial closing (for insured advances projects) or issuance of the Firm Commitment (for insurance upon completion projects); and/or
2. The Contractor used the Construction Contract-Cost Plus, Form HUD-92442M, whether or not any identity of interest with the borrower existed or developed.

C. When the Borrower is required to cost certify subcontractors at any tier, equipment lessors, material suppliers and manufacturers of industrialized housing must cost certify where:

1. The total of all subcontracts, purchases, and leases are more than 0.5% of the mortgage, and
2. An identity of interest exists or comes into being between such subcontractor, equipment lessor, material supplier, or manufacturer of industrialized housing and either:
   a. The borrower, or
   b. The contractor where the contractor must cost certify.

13.7 Cost Certification Sequence of Events

A. Notification of Pre-Cost Certification Conference. HUD must notify the mortgagee, borrower, and contractor when the project is 80% complete. HUD should notify new sponsors and general contractors as early as 70% completion. The letter should state that:

1. The borrower, general contractor, their accountants, and the mortgagee should attend the conference.
2. Enclose with the letter the (800) 767-7468 number or the internet address for:

a. Handbook IG 2000.4 Consolidated Audit Guide for HUD Programs: http://www.hud.gov/offices/adm/hudclips/handbooks/oigh/.

b. Four copies of each of the applicable forms (www.hud.gov):

(1) Form HUD-92330, Borrower's Certificate of Actual Cost.

(2) Form HUD-92330A, Contractor's Certificate of Actual Cost, if applicable.

B. Conduct of conference is the responsibility of the assigned HUD staff and should be held before the project is 90% complete. At the conference, HUD staff will explain:

1. Substantial completion, administrative completion, and cut off dates.
2. Documentation required for cost certification including the income statement and balance sheet.
3. Remind the borrower and accountant that they are responsible for computing the liquidated damages/actual damages and incentive portions, if applicable, of the construction contract using the certified amounts on Form HUD-92330.
4. Necessity for a careful review and completeness of the documentation including dates and signatures, and timeliness of the submission, HUD review, and final endorsement.
5. Any problems with prevailing wage certifications or other labor issues.

C. Cut-off date established for computation of the cost certification. Submission and HUD approval of the cost certification must occur before final closing, except that the Section 223(f) supplemental cost certification is not required until completion of non-critical repairs deferred until after closing.

E. Upon completion of the project, Form HUD-92464M, Request for Approval of Advance of Escrow Funds, should be prepared by the Lender and submitted to HUD for approval.

13.8 Substantial Completion Date, Cut-Off Date, and Final Completion Date

A. Completion dates.

1. The substantial completion date for determining actual costs is the date the Architect dates and signs the certification on Form HUD-92485, Permission to Occupy Project Mortgages. The Architect is certifying that part of or all of the construction work is sufficiently complete in accordance with the construction contract documents and that the project may be occupied for the intended use. The form is subsequently signed by HUD's Authorized Agent. Construction must be complete except for acceptable items of delayed completion and the Hub/PC will notify the borrower, general contractor, and mortgagee, in writing, of the substantial completion date.

2. The substantial completion date is the effective date for cost certification. The borrower has the option to include in the cost certification all soft costs incurred up to 60 days beyond this date. The date selected by the borrower is the "cut-off date" for the soft costs.
3. The borrower's balance sheet and operating statement date must agree with the selected cut-off date.
4. The final completion is the date the HUD Inspector signs the final HUD Representative's Trip Report, Form HUD-95379, provided that the Construction Manager subsequently endorses the trip report. Construction must be 100% complete.

5. For financial reporting purposes, the day after the cut-off date is the commencement of operations and the projects' first year annual audited financial statements, which will cover the period from the day after the cut-off date to the projects' fiscal year end. This is the date AM will start monitoring the project's financial condition (monthly accounting reports) once the certificates of occupancy (Form HUD-92485) are issued.

13.9 Administrative Completion Date

The Hub Director may advance the completion date to prevent unnecessary accumulation of soft costs when projects which are nearly complete face unnecessary delay.

A. The Hub Director may set an administrative completion date for any project when the monthly inspection reports show 95% completion of work and thereafter less than 2% increase in percentage of completion in any month.

B. The Hub Director will notify the borrower, general contractor, and mortgagee in writing of the administrative completion date and the following:
   1. The administrative completion date is the effective date for cost certification except that all soft costs up to 60 days beyond this date may be included at the option of the borrower.
   2. The date of the balance sheet and operating statement must be the same as the cut-off date selected by the borrower.
   3. Liquidated/actual damages for cost certification purposes will be computed using the administrative completion date. However, the general contractor is responsible for liquidated/actual damages through the date of substantial completion.

C. Copies of the notification go to the HQ Docket, Office Docket, and Closing Attorney's file.

13.10 Submission Date

The submission date for cost certification should be within 30 to 45 days after the cut-off date, and not less than 30 days before the desired final closing date.

13.11 Required Forms

A. Form HUD-92330, Borrower's Certificate of Actual Cost; see line-by-line instructions contained in the Forms Book or on the multifamily internet site: http://www.hud.gov/offices/adm/hudclips/index.cfm.

B. Form HUD-92330A, Contractor's Certificate of Actual Cost; see line-by-line instructions contained in the Forms Book. The subcontractor, material supplier, industrialized housing manufacturer, and the equipment lessor are required to use this form to certify cost.

   Note: When a project includes rehabilitation and new construction, a separate form is required for each, with a master form summarizing total project costs, including fees.

C. Form HUD-2205-A, Borrower's Certificate of Actual Cost (Section 207 Pursuant to Section 223(f)), and line by line instructions are contained in the Forms Book or on the multifamily internet site http://www.hud.gov/offices/adm/hudclips/index.cfm.

13.12 Required Statements and Certifications

For all projects, regardless of whether the project has a cost certification exemption, the required statements and certifications are:

B. New construction - an unaudited balance sheet that covers the period from the date of initial endorsement through cut-off and an unaudited income statement that covers the period from the date of initial occupancy through the cut-off date. The format and content of the balance sheet must follow Section 13.12.B.4 & B.5, below.

C. Substantial rehabilitation – an unaudited balance sheet and an unaudited income statement that date from the date of initial endorsement through the cut-off date. The format and content of the balance sheet must follow Section 13.12.B.4 & B.5, below.

Follow either A or B, below, depending on qualifications in A.1.

A. Simplified Form of Cost Certification. Use Forms HUD-92330, HUD-92330A (if a cost plus construction contract was used or an identity of interest exists between the borrower and the general contractor). An accountant's opinion is not needed.

1. Simplified cost certification is permitted for new construction or substantial rehabilitation projects involving 40 units or less and for refinancing or purchase of existing properties under 207/223(f).
2. If there is an identity of interest between a subcontractor, material supplier, equipment lessor, or manufacturer of industrialized housing and the borrower and/or general contractor who must cost certify, and the total of all identity of interest subcontracts, purchases and leases is more than 0.5% of the mortgage, the identified party uses Form HUD-92330A. This requirement established by the Agreement and Certification, Form HUD-93305M, applies in all cases.
3. An un-audited balance sheet of the borrower entity, as of the cut-off date is required in all cases. Format and content of the balance sheet must follow Section 13.12.B.4, below.
4. An un-audited operating statement is required if occupancy occurred during construction. Format and content of the operating statement must follow Section 13.12.B.5, below.

B. Long Form Cost Certification. For cases that do not qualify for simplified cost certification based upon paragraph A.1, above, please submit the following:

1. Borrower's Certificate of Actual Cost, Form HUD-92330, supported by an accountant's opinion (refer to Section 13.12.B.6).
2. Contractor's Certificate of Actual Cost, Form HUD-92330A, supported by an accountant's opinion (refer to Section 13.12.B.6), is required if there is an identity of interest with the borrower or if a cost plus construction contract was used.
3. Subcontractors, suppliers, and equipment lessor with an identity of interest with either the borrower or general contractor must submit Form HUD-92330A supported by an accountant's opinion.
   a. Material suppliers. Attach to Form HUD-92330A a sheet showing:
      (1) Quantities furnished.
      (2) Sources from which the materials were obtained.
      (3) Unit prices paid to the sources, brand names, model numbers, sizes, lumber grades, etc., as applicable.

      <u>NOTE</u>: No amount will be included for general requirements (ie: job overhead).
   b. Equipment Lessor. Attach to Form HUD-92330A a sheet showing:
      (1) Dates the equipment was acquired,
      (2) Age of equipment at acquisition date,
      (3) Brand names and model numbers,
      (4) Sizes,

(5) Dates and length of time used, and

(6) Rates charged.

(a) The Lessor(s) must certify that:

(i) The rates charged were not more than the local going rate obtainable in the area, including any maintenance and repair.

(ii) The time charged was not more than essential for the project.

(iii) The charges did not exceed the purchase price of the equipment.

(b) Lump Sum Basis. Instead of providing an attachment containing the above information, the lessor(s) may elect to certify to charges at 85**%** of the local going rates for identical equipment under arms' length (lump sum) leases. When using this alternative, the lessor agrees**:**

(i) The Hub is the sole judge of the reasonableness of the time and rates charged, and

(ii) Equipment maintenance and repair expense is the responsibility of the lessor(s) and is not included as an additional cost.

(c) Subcontractor's equipment. Costs for subcontractor(s) equipment, whether owned or rented, are considered in the markup for overhead and profit. These costs shall be reflected in the total subcontract and in the prior approval of identity of interest entities. A separate certification of the equipment is not required.

(d) Manufacturer of Industrialized Housing. Attach to Form HUD-92330A, a breakdown of Division 13, Special Construction showing:

(i) Manufacturing costs.

(a) Labor

(b) Materials

(c) Sales and any other taxes

(d) Factory overhead

(e) General overhead and profit

NOTE: The manufacturer's accounting system must follow generally accepted accounting procedures, which will allow certification of the actual cost of manufacturing by a Certified Public Accountant or Independent Public Accountant. No amount will be included for transportation or work at the project site.

(ii) Transportation costs, factory to project site (if provided by manufacturer).

(a) Labor

(b) Equipment

(iii) On-site erection costs (if provided by manufacturer).

(a) Labor

(b) Equipment

(c) Materials

(d) General requirements (job overhead)

(iv) The remainder of the manufacturer's Form HUD-92330A is completed per outstanding instructions.

NOTE: There can be no duplication of manufacturing costs, i.e., repair of components damaged in shipment.

4. An audited balance sheet of the borrower entity, as of the cut-off date is required.

   a. The balance sheet must contain the following certification:

      I HEREBY CERTIFY that the foregoing figures and statements contained herein submitted by me as agent of the borrower [owner] for the purpose of obtaining mortgage insurance under the National Housing Act are true and give a correct showing of (Name of borrower or owner) financial position as of (date of financial statement).

      Signed this ____day of _____, 20XX_____ (Signature of authorized agent with name printed or typed under signature)

      WARNING: HUD will prosecute false claims and statements. Conviction may result in criminal and/or civil penalties. (18U.S.C. 1001, 1010. 1012; 31U.S.C. 3729, 3802)

   b. Furnish reconciling information if short-term liabilities on the balance sheet do not agree with Column B of Form HUD-92330.

   c. Explain the purpose of all liabilities in the notes to the financial statement and include repayment requirements of the liabilities. Take special care to note any liabilities included for repayment on the balance sheet that were not disclosed during the firm processing stage or before initial endorsement. If such liabilities are found, inform the borrower that the liabilities cannot be an obligation of the project; repayment is the responsibility of the borrower. These liabilities will not be considered (allowed nor disallowed) in the review of the cost certification. When non-disclosures are found it requires a detailed review of cost certification Forms HUD-92330 and HUD-92330A.

   d. If proceeds and obligations from project syndication are passed through the books and records of the borrower entity, reflect receivables as an asset of the borrower entity.

   e. The notes to the balance sheet must identify the original amount of and summarize the expenditures from the working capital deposit.

5. An audited operating statement is required if occupancy occurs before the cost certification cut-off date.

a. The statement must contain the certification contained in Section 13.12.B.4.

b. Prepare the operating statement on an accrual basis.

c. The statement covers the beginning of marketing and rent-up activities (or date of initial endorsement in rehabilitation projects where occupancy is continuous) to the cut-off date.

d. Marketing and rent-up activities will start no later than 6 months before the issuance of the first Permission to Occupy-Project Mortgages, Form HUD-92485.

e. The statement must show the actual dates covered rather than language such as "From the Date of Commencement of Marketing and Rent-up Activities, etc."

f. The statement must show income from all sources. Do not consider security deposits as income.

g. The operating statement should not contain any expense items that were paid or should have been paid from the working capital deposit or otherwise included in cost certification.

h. Operating expenses may include:

(1) Expenses directly relating to renting the project, such as:

(a) Rental commissions customary for the type of project, if any, and

(b) Marketing and advertising expenses.

(2) Purchase of furnishings, equipment not paid from the working capital deposit, and supplies essential to project operation.

(3) Reasonable fees for preparing any Federal, State, or local tax return information required of the project.

(a) For example: If the borrower entity is a partnership, the cost of preparing both Form 1065, U.S. Partnership Return of Income, and related K Schedules may be considered. Do not recognize the cost of preparing a partner's personal Form 1040 return.

(b) For projects owned by an individual include the cost for preparing any tax return schedule related to project operations; but do not other parts of the owner's return.

(4) Electricity, gas, water, and operating salaries (maintenance, cleaners, gardeners, elevator operators, etc.) to the extent they are not included in construction cost of Form HUD-92330, Borrower's Certificate of Actual Cost, or HUD-92330A, Contractor's Certificate of Actual Cost.

(5) Management fee stated in the contract.

(6) Services not covered by the management fee under Chapter 3 of Handbook 4381.5, Compensations for Management Services in Multifamily Housing Projects with Insured or HUD-Held Mortgages.

i. Operating expenses may not include:

(1) Depreciation

(2) Interest, taxes, property insurance premiums, and mortgage insurance premiums that are reflected in Form HUD-92330, Borrower's Certificate of Actual Cost.

(3) Salaries paid to principals of the sponsor or borrower for managing the borrower entity.

j. Treatment of net operating income generated during construction:

(1) If the replacement cost mortgage (Criterion 3) is not the controlling mortgage, any NOI generated during construction may be applied to cover shortfalls in mortgageable soft costs, change orders, initial operating deficit and escrows. At Final Endorsement the balance of funds may be distributed to the borrower or deposited to the project's Reserve for Replacement account or applied toward the amortization of the mortgage principal.

(2) If the replacement cost mortgage (Criterion 3) is controlling the Mortgage Credit staff will do a calculation and determine if the balance of the net operating income is equal to or greater than 1% of the original mortgage amount, and if it is, will deduct this amount from the certified replacement cost. When the NOI does not meet this 1% threshold, it can be used toward shortfalls as instructed in number 1 above. Any remaining balance must be deposited into the project's Reserve for Replacement account at final endorsement. There is no distribution to the borrower.

(3) For a nonprofit mortgagor processing under the 221(d)(3) program:

(a) As a recovery of construction costs at cost certification, to the extent that it was used to reduce liquidated/actual damages.

(b) As an offset for a mortgage increase.

(c) Deposit the unused portion of net income into the project's Reserve for Replacement account at final endorsement.

k. If operating expenses exceed income:

(1) No entry is made on Form HUD-92330, Borrower's Certification of Actual Cost.

(2) Operating deficit may be carried over as a reduction to net income on the supplemental operating statement.

6. A Certification by an independent Certified Public Accountant or an Independent Public Accountant must accompany Form HUD-92330, Borrower's Certificate of Actual Cost, including the audited balance sheet and operating statement of the borrower, and Form HUD-92330A, Contractor's Certificate of Actual Cost.

a. The accountant must meet the auditor qualifications of the Government Auditing Standards (GAO Yellow Book), including the qualifications relating to independence and continuing

professional education. The audit organization also must meet the quality control standards of the GAO Yellow Book.

b. Part 24 of Title 24 of the Code of Federal Regulations prohibits accountants from contracting for services when their name is shown on the HUD and General Services Administration Government-wide Consolidated List of Debarred, Suspended and Ineligible Contractors and Grantees.

c. The accountant must also comply with the requirements in Chapters 1, 2, and 6 of HUD Handbook IG 2000.4, "Consolidated Audit Guide for Audits of HUD Programs."

7. The borrower must submit a supplemental operating income statement if more than 3 months exist between the cut-off date and the start of amortization. If a deferment of amortization was granted, (Section 13.26) use the new date for the start of amortization in determining the need for a supplemental operating statement.

a. This requirement does not apply to nonprofit borrowers or any project where the mortgage is $200,000 or less.

b. The statement covers the period from the cost certification cut-off date to the date, which is 3 months before the start of amortization. The borrower should submit the statement within 30 days after the expiration of this period.

c. If the required original cost certification was audited, a CPA or IPA must prepare and certify the supplemental statement.

d. The borrower may advance the date of amortization to avoid submitting a supplemental income statement.

e. In preparing the statement, if the operating statement submitted at cost certification shows expenses in excess of income, such expenses may be carried forward as "un-recovered expense–prior period."

C. Section 223(f) Projects. The borrower must certify to the total costs incurred in the acquisition or refinancing of the property using Form HUD-2205-A, Borrower's Certificate of Actual Cost. The certification must be dated and signed by an authorized agent of the borrower. An accountant's opinion is not needed.

1. The certification must be submitted after all critical repairs have been completed, but at least 15 days before the desired closing date.

2. The general contractor will be required to cost certify using Form HUD-92330A if a cost plus construction contract is used.

3. A balance sheet and income statement are not required.

4. No cost certification is required for a 207/223(f) refinancing transaction where the mortgage is equal to or less than 80% of value.

5. For cases involving deferred repairs, the borrower must submit a supplemental cost certification (Form HUD-2205-A) detailing the actual cost of the deferred repairs.

13.13 Deficiencies in Cost Certification Submission

When the cost certification package is received for processing:

A. The Cost and Mortgage Credit reviewers will:
   1. Determine deficiencies associated with the borrowers' and contractor's cost certifications.
   2. Advise the Hub Director and estimate the time needed to resolve the problem(s).
   3. Attempt to resolve all problems by telephone before making a formal written request. This usually allows processing to continue while waiting for a formal reply.
   4. Send a letter within 5 workdays to the borrower with copies to the general contractor (if applicable), their accountants, and the mortgagee stating the deficiencies and requesting information.

B. Upon receipt of all necessary information, combined processing should not exceed 15 workdays.

C. If the borrower or contractor indicates clarification will be forwarded within 5 work days, the conclusions of cost certification can await the additional information.

D. If not, issue Form HUD-92580.

13.14 Mortgage Credit Limited Review

A. In cases where the borrower has not requested a mortgage increase, the HUD staff will:
   1. Review Form HUD-92330, Borrower's Certificate of Actual Cost. Adjust for items paid out of working capital and costs reflected on income statement.
   2. Review the reporting of:
      a. Net income earned before the start of amortization. Report all income earned from the beginning of marketing and rent-up activities to the cut-off date for new construction projects and unoccupied substantial rehabilitation projects. For substantial rehabilitation projects where occupancy is continuous, report all income from the date of initial endorsement or, for insurance upon completion cases, the start of construction to the cut-off date. Make adjustments for ineligible reported expenses, such as depreciation.
      b. The reporting of all grants/loans received for replacement cost items.
   3. Complete Form HUD-92580, Maximum Insurable Mortgage, using the figures from Column C, Total, of Form HUD-92330. Complete the forms using the instructions in the MAP Forms Book, except for the following changes:
      a. Line 2. Reflect the amount indicated in Column C of Form HUD-92330.
      b. Line 3. Explain any adjustments made to the net income or grant/loan amounts reported on Form HUD-92330.

NOTE: If adjustments are made to items other than net income and grants/loans, Form HUD-92331A should be completed.

4. When the borrower and the contractor submit their individual certificates of actual costs for review they should have already agreed to the amount due the contractor. The amount due the contractor is reported on the certificates of actual costs and there should no disagreement because all "to be paid items" will be listed on the HUD-92580 schedule 1, item by item. The Form HUD-92023, Request for Final Endorsement of Credit Instrument, must match the Maximum Insurable Mortgage, HUD-92580 minus whatever was paid in the interim. As mortgage credit performs the cost certification and prepares the HUD-92580, consider the follow when reconciling the certified costs:
   a. After completion of the 92580 the Hub/PC notifies the Lender/Owner/GC of the balance in the line item for the G.C., if there are issues then the Field will not move forward with the cost certification until all pending "to be paid items" are resolved.
   b. The GC's cost certification has to balance with the items remaining to be paid.
   c. Mortgage Credit has to reconcile these numbers at cost certification, if there is a dispute all releases freeze until HUD/Lender/GC come to agreement on who is owed what.
5. Report anything suspicious in the submission, (i.e. liabilities not disclosed during firm processing or before initial endorsement) to the Hub Director, who has the authority to request that a full cost certification review be completed. For such cases, complete Forms HUD-92331-A, and HUD-92580 based on the instructions in the Forms Book or on the multifamily internet site http://www.hud.gov/offices/adm/hudclips/index.cfm, and Section 13.16, below. Also, if an accountant's work is consistently deficient, warn the accountant that borrowers using their services will be advised that HUD will perform a detailed cost certification review.

13.15 Mortgage Credit Detailed Review

When a mortgage increase is requested of the Hub Director, a more detailed review is required. The HUD Mortgage Credit staff will:

A. Carefully review Forms HUD-92330 and HUD-92330-A if required for mathematical accuracy and compliance with prescribed procedures.

B. Ensure that the submission contains required schedules and bills, which have not been submitted with previous draw requests, to support the certified amounts for interest, taxes, property insurance, MIP, title and recording, financing fees, legal, organizational and audit fees, offsite costs and other fees.

C. Require clarification or breakdown of all, or any part of, the cost figures presented by the borrower or general contractor, if applicable.

D. Scrutinize any existence of an identity of interest subcontractor, material supplier or equipment lessor relationship.

E. Review the notes and schedules attached to the accountant's opinion. Pay special attention to any liabilities included for repayment on the balance sheet that were not disclosed during the firm processing stage or before initial endorsement. These liabilities are not eligible for inclusion in the cost certification.

F. Recommend that the Hub Director request an audit of the borrower's and/or contractor's books by the Regional Inspector General for Audit before issuing Form HUD-92580, Maximum Insurable Mortgage, when differences of opinion arise from other than:

   1. Honest differences of opinion clearly identifiable as such.
   2. Other justifiable causes.

G. If considerable time has passed between initial occupancy and the cut-off date, some items properly allocable to renting and operating the project may be charged against construction cost.

   1. It may not be possible or practical to make precise allocation of such items as gas and electricity, clean-up costs, etc., between construction and operation periods.
   2. Insist on reasonable allocations and eliminate duplicate claims for the expenses under both categories.

H. Advise cost staff of any construction costs included in "Miscellaneous" and "Other" categories of Form HUD-92330.

I. Check items and amounts in the borrower's cost certification without auditing the borrower's books and records. An audit may be needed later. (Refer to Section 13.27)

J. Record the results of the review (including NOI) on Form HUD-92331A, Cost Certification Review Worksheet.

13.16 Allowable Costs in Borrower's Certificate of Actual Cost

A. Construction Contract:

   1. A lump sum construction contract is permitted when no identity of interest exists between the borrower and general contractor. The amount allowed in cost certification is the lesser of:

      a. Actual cash paid or to be paid by the borrower under the construction contract.
      b. Contract price as adjusted by HUD's estimated cumulative effect of approved change orders paid, or to be paid, by the borrower and the liquidated/actual damages provision to the contract, if applicable.

2. A cost-plus construction contract is required when an identity of interest exists between the borrower and general contractor.
3. The amount allowed in cost certification when a cost-plus contract is used is the lesser of:
   a. Actual cash paid, or to be paid, by the borrower under the construction contract.
   b. Amount the cost analyst allowed for construction on Form HUD-92331, Summary of Cost Certification Review–Cost Section.
   c. Contract price as adjusted by the HUD estimated cumulative effect of approved change orders paid, or to be paid, by the borrower and, if applicable, either the incentive provision or the liquidated/actual damages provision of the contract.

      NOTE:

      (1) Recognize approved change orders necessitated by errors or omissions by the architect only to the extent there are savings in the mortgage. Do not recognize these change orders when processing a mortgage increase.

      (2) Do not recognize approved betterment change orders in calculating the adjusted upset price in paragraphs A.1.b and A.3.c, above, unless they are determined by the cost staff to be necessary changes as defined in Section 12.8.

      (3) Recognize the increase in general requirements, if any, noted on approved time extension change orders. Do not recognize increases in soft costs associated with the change order. The soft costs will be recognized under the applicable line items.

      (4) When BSPRA is not applicable, for profit motivated projects involving an identity of interest between the borrower and general contractor, the amount of builder's profit as shown on Form HUD-93305M is eligible whether or not it was paid in cash.

      (5) For nonprofit borrowers, the allowable builder's profit is the lesser of the amount actually paid or to be paid in cash to the general contractor or the amount of builder's profit shown in Section G of Form HUD-92264, plus or minus any amount applicable due to HUD-approved change orders.
4. An identity of interest is construed to exist when:
   a. There is any financial interest of the borrower in the general contractor or any financial interest of the general contractor in the borrower.
   b. Any officer, director, or stockholder or partner of the borrower is also an officer, director or stockholder or partner of the general contractor.
   c. Any officer, director, stockholder, or partner of the borrower has any financial interest in the general contractor; or any Officer, director, stockholder, or partner of the general contractor has any financial interest in the borrower.
   d. The general contractor advances any funds to the borrower.

e. The general contractor supplies and pays, on behalf of the borrower, the cost of any architectural services or engineering services other than those of a surveyor, general superintendent, or engineer employed by a general contractor in connection with its obligations under the construction contract.

f. The general contractor takes stock or any interest in the borrower corporation as consideration of payment.

g. There exists or comes into being any side deals, agreements, contracts, or undertakings entered into or contemplated, thereby altering, amending, or canceling any of the required closing documents, except as approved by the Secretary.

h. Any relationship (e.g. family) existing which would give the borrower or general contractor control or influence over the price of the contract or the price paid to the subcontractor, material supplier or lessor of equipment.

5. Incentive Fee Payments to Contractors.

The owner may request that the construction contract be modified before Initial Endorsement to provide for a general contractor incentive fee for completed construction work and delivering a completed project before the date specified in the construction contract (or as amended by HUD-approved time extension(s)). Incentive fees must be specified in an Addendum to the construction contract that has been approved by HUD before initial endorsement or at the execution of a construction contract that has been approved by HUD for Insurance Upon Completion and Insurance of Advance projects. An Incentive Payment Addendum may not be added to the contract after Initial Endorsement.

a. Identity of interest borrower and general contractor.

(1) General contractor may benefit from savings in construction interest, taxes, property insurance, and mortgage insurance premiums to the extent there are construction cost overruns.

(2) Incentive payment is included in the adjusted upset price of the construction contract.

If there is an identity of interest between the borrower and the general contractor, an incentive fee may only be paid if there are certified cost overruns that were not included in a HUD approved change order, and the amount of the incentive fee may not exceed the amount of certified cost overruns that were incurred

b. Nonidentity of interest borrower and general contractor.

(1) Use Construction Contract Incentive Payment, Form HUD-92443.

(2) Include the incentive payment under “Other” on Form HUD-92331A.

Incentive fees must be calculated in accordance with Form HUD-92443. The incentive fee computed for Lump Sum construction contracts may not exceed 50% of the amount by which the estimated interest, taxes, property insurance and mortgage insurance premium, exceeds the certified costs for these same items through the actual date of completion.

The incentive fee computed for Cost Plus construction contracts may be paid in an amount calculated in accordance with the Incentive Payment Computation on page two of Form HUD-

92443. Additionally, when the cost plus contract is used the **contractor may not** receive total payments that exceed: (1) the actual costs of construction, (2) the cash fee provided in the construction contract, or (3) the incentive fee as determined by the computation. (The contractor shall not be paid an incentive fee that is greater than the amount of cost overruns; the contractor must only receive the amount of the incentive fee. Any excess of this amount must be refunded to the borrower.)

6. Damages Clause. Apply the damages clause of the construction contract when the general contractor does not complete the project on time. The clause holds the general contractor financially responsible for the added soft costs resulting from the contractor's delay.
   a. Calculate the amount of actual damages and liquidated damages, using the lesser to determine the adjusted upset price.
   b. To determine actual damages, compute the actual cost of interest, taxes, insurance, and MIP for the period from the scheduled completion date (as amended by HUD-approved change orders) through the substantial completion date.
   c. To determine liquidated damages multiply the daily liquidated damages rate from the construction contract by the number of days between the scheduled completion date specified in the construction contract, as amended by the HUD-approved time extensions, through the substantial completion date.
   d. Reduce the damages by the portion of the net operating income earned during the liquidated/actual damage period.
   e. For those cases where an administrative completion date has been established, use this date for computing damages for cost certification purposes. However, the general contractor is responsible for damages through the date of substantial completion.
7. If a borrower acts as its own general contractor:
   a. A construction contract is not executed. Instead, Form HUD-92441M-Supplement is added to the Building Loan Agreement, Form HUD-92441M.
   b. The upset price for construction is line 51 of the approved Form HUD-2328, Contractor's and/or Borrower's Cost Breakdown (Schedule of Values), as adjusted by the cumulative effect of HUD-approved change orders and the incentive provision, if applicable.
   c. Incentive clause, if any, is incorporated by addendum to Form HUD-92441M-Supplement.
   d. There is no liquidated/actual damages clause.

      NOTE: The borrower may serve as its own general contractor only when the borrower is an individual or a general partnership.
8. Incomplete Minor Items. The borrower's certification of the amount due under the terms of the construction contract may include the cost of minor items of on-site work that remain incomplete under the construction contract.

B. Architect's fee(s) are limited to the amounts paid in cash.

1. Recognize the cost of additional services set form in Article 10 of the Standard Form of Agreement between Owner and Architect for Housing Services, AIA Document B108. Ask Architectural and Cost staff to check the reasonableness of these charges.
2. Disallow:
   a. Any portion of the Architect's fee paid in stock.
   b. Any costs associated with a clerk of the works.
3. If any identity of interest comes into being between the Architect and either the borrower or general contractor during project construction:
   a. See maximum design Architect's fee for cost certification purposes set forth in the Agreement and Certification, Form HUD-93305M.
   b. Do not allow a fee for supervisory services to an identity of interest Architect.
4. Treat any unused balance of the total Architect's fee as a direct mortgage reduction to the original mortgage amount on Form HUD-92580.

C. Interest is allowable in the amount accrued on the first mortgage between initial endorsement (start of construction for insurance upon completion projects) and the cut-off date defined in Section 14.7.

1. Recognize interest costs associated with an approved early start provided:
   a. The borrower entered into an agreement with the contractor which:
      (1) Was approved by the Hub Director.
      (2) Agrees to reimburse the contractor for interest on money borrowed for construction prior to initial endorsement.
      (3) States that reimbursement will be made only to the extent the borrower has funds available in the amount estimated for interest during construction.
   b. The certified amount, when added to the interest cost incurred directly by the borrower, does not exceed the total amount of interest estimated in Section G of Form HUD-92264.
   c. Form HUD-92415, Request for Permission to Commence Construction Prior to Initial Endorsement for Mortgage Insurance, was executed and approved.
   d. Interest costs reflect the contractor's actual cost of money borrowed to cover the cost of construction between the early start date and the initial endorsement as adjusted by paragraph e., below.
   e. Rate of interest does not exceed the rate established for the insured loan.
2. Interest rate paid on the construction loan cannot exceed:
   a. For insurance of advances: the rate stated in the Firm Commitment.
   b. For insurance upon completion: the rate acknowledged by the Hub Director before issuing the Firm Commitment.
3. Deduct accrued interest forgiven by the Lender or otherwise not paid in cash.

4. Treat Lender/bond underwriter's refund of any portion of the construction loan interest to the borrower or sponsor, as a direct mortgage reduction to the original mortgage amount on Form HUD-92580.
5. If the construction interest rate changes before initial endorsement and it was not feasible to reprocess the project or if tax exempt bonds were sold to finance the construction loan and the true interest rate was not known until cost certification:
   a. Interest savings may be created from the difference between the processed interest rate and the actual final interest rate.
   b. Treat these savings as a direct mortgage reduction if the following condition was included in the firm commitment:

      "Any interest savings resulting purely from a differential between the HUD processed interest rate and the actual construction interest rate may not be construed as excess funds that may be used to offset costs in other categories at the time of cost certification. Any such saving must be applied as a mortgage reduction."
6. Neither the interest on subordinated liens nor other obligations of the borrower are allowed as certifiable costs.

D. Taxes are allowable in the amount accrued on the first mortgage between initial endorsement (start of construction for insurance upon completion projects) and the cut-off date defined in Section 13.7. Do not recognize costs accrued during the early start period.

E. Property insurance is allowed in the amount accrued on the first mortgage between initial endorsement (start of construction for insurance upon completion projects) and the cut-off date defined in Section 13.7. Do not recognize costs accrued during the early start period.

F. MIP. The FHA Comptroller's office cannot compute the exact amount of MIP due during the construction period until the project has been completed and the Washington Docket forwarded to Headquarters.
   1. For a project involving insurance of advances, allow MIP of 0.5% per annum on the mortgage amount on the basis of accrual for the number of days in the period used to Paragraph C above, when applicable.
   2. For a project involving insurance upon completion, no MIP is paid during construction.

G. HUD application, commitment and inspection fees are allowable in the amounts paid. Fees paid to reopen an expired or terminated commitment are not allowable costs.

H. Financing expense includes the initial service charge, discounts fees, GNMA, permanent Lender commitment fees, and other similar fees.
   1. Allow the lesser of:
      a. Amounts paid, or to be paid, in cash.

b. Amounts shown on Form HUD-92434M, Lender's Certificate (formally Mortgagee's Certificate), or Certificate of Mortgagee portion of Form HUD-92455M and approved by the Hub Director before Initial Endorsement (Insurance of Advances) and issuance of Firm Commitment (Insurance Upon Completion), respectively.

2. Construction Lender's initial service charge (usually 2%):

   a. Is expected to cover:

      (1) Processing fees.

      (2) All expenses of the Lender's counsel paid directly from the initial service charge. (Reconcile separate invoices or bills with the cost of the itemized figures.)

      (3) All other charges by the construction Lender.

   b. Excludes:

      (1) Construction loan discount.

      (2) Construction loan extension fees.

   c. Any charges made by the Lender for payment of counsel services or charge paid directly to the Lender's counsel, to the extent they cause the initial service charge to exceed 2 percent, are not certifiable. Except, if charges are related to "Title and Recording" expenses certify it under Section 13.15.I below.

3. Permanent Lender's placement fee (usually 1.5%):

   a. Is expected to cover all permanent placement expenses except discounts and some of the fees associated with a bond financed transaction.

   b. If GNMA Mortgaged Backed Securities are involved, the mortgagee may not assess an additional charge for the MBS application fee or for the custodial or delivery fee.

      NOTE: Construction and Permanent Lenders' fees in the aggregate shall not exceed 3.5% (5.5% for bond financed projects) and the parties involved can divide the fees as agreed.

4. Recognize for cost certification:

   a. Reasonable discounts based on current interest rates at the time of issuance of the Firm Commitment for projects involving insurance of advances and insurance upon completion charged by the construction and permanent Lenders. Recognize extension fees charged by the construction Lender if funded at initial endorsement and shown on the Lender's Certificate, Form HUD-92434M (formally Mortgagee's Certificate).

   b. Permanent Lender extension fees, shown on Form HUD-92434M, if funded before the substantial completion date.

   c. For Insurance Upon Completion cases, construction and permanent loan extension fees, shown on the Certification of Mortgagee portion of Form HUD-92455M, if funded before cost certification cut-off.

   d. Financing fees (including extension fees and discounts) paid on behalf of a borrower by a third party under Paragraph 18(f) of the Mortgagee's Certificate or Paragraph 10h of Certificate of Mortgagee portion of Form HUD-92455M and shown as a current liability on

the borrower's balance sheet to the extent there are savings in the mortgage. At final endorsement, require a promissory note be used for any unpaid balance of the obligation recognized in cost certification.

e. For bond financed projects, cost of issuance, discounts, and financing fees in excess of 5.5%; provided the cost certification evidences that the sponsor/borrower cannot benefit monetarily from excess investment income from the proceeds of the invested obligations. Refer to Section 8.15.

5. Do not recognize for cost certification:
   a. Any "side deals" (except for approved discounts) by which the borrower agrees to pay additional sums.
   b. The 4% construction loan and 1.75% permanent loan GNMA indemnification escrows.
   c. Discounts required to buy down the construction and/or permanent rate to a below market rate.
6. Treat the following as a direct mortgage reduction at final endorsement:
   a. Premiums paid by Lender to the borrower or sponsor for acquiring the construction or permanent loan.
   b. Partial refunds of the Commitment fee allowed in processing, which are returned to the borrower or sponsor.
   c. Discounts or other fees paid for by a contribution of a portion of the initial service charge by the Lender/bond underwriter.
   d. Rebates paid to a borrower or sponsor by the Lender/bond underwriter for bond -financed mortgages.

I. Title and recording expense is limited to cash paid for:
   1. Title search and policy at the time of initial endorsement;
   2. Recording fees at initial endorsement;
   3. Mortgage and stamp taxes;
   4. Survey recording fees;
   5. Updating title policy during construction;
   6. Final title policy and recording charges; and
   7. Legal fees incurred with any of the above.

J. Legal, organization and audit expenses are limited to expenses incurred in organizing the borrower entity, developing the proposal to submit to HUD and other necessary governmental agencies and required services during closing and construction.
   1. Organizational allowance:

a. Allow only the amount included in Section G of Form HUD-92264 for the organizational fee, unless the borrower, which justifies the need for, and reasonableness of the additional expenditure submit fully supporting documentation.

b. Any costs incurred in excess of this allowance are not eligible for recognition in processing a mortgage increase or the equity computation on Form HUD-92580.

2. Limit the Borrower's legal expenses to those incurred for: initial through final closings, tax advice during organization of borrower entity only, and preparation of documents and representation for and during organization of the borrower entity.

   a. Allow customary expenditures expected to be incurred before and during initial closing, construction period, and final closing.

   b. Do not allow:

      (1) Expenses connected with land acquisition which is already included in, or contributing to:

         (a) Title and recording expense.

         (b) Estimated market price of site.

         (c) Obtaining changes in zoning.

      (2) Cost of legal services to create tax shelters, trusts, etc.

3. Recognize cost of a "package deal" for organization and legal services provided:

   a. Supplier is qualified to furnish the needed services.

   b. Do not allow duplicate credit for the same services.

4. Audit fee covers the cost of the accountant's audit and opinion of the borrower's certificate of costs.

5. Amounts included in Form HUD-92264 for legal and audit expenses are not blanket allowances, but ordinarily set an upper limit on allowable amounts.

   a. Non-typical fees must be borne by the borrower, unless in an exceptionally complex case, a higher fee is proven by the borrower to be necessary and reasonable. Detailed invoices and/or other documentation is required as to the reasonableness, purpose, necessity and proper classification of all items in the category.

   b. This limitation is not flexible where a "package" for legal and organizational services is involved or where a substantial amount of the legal and organizational services are performed by the same firm.

K. Offsite Costs. Where the borrower enters into a supplemental contract for constructing offsite improvements, allow the lesser of:

1. Contract price as adjusted by the HUD's estimated cumulative effect of approved offsite change orders.

2. Actual cash paid or to be paid for offsite work.

3. Amount allowed by cost analyst for offsite construction of Form HUD-92331, Summary of Cost Certification Review - Cost Section.

   NOTE:

   a. The Valuation Branch must adjust the as-is land value of the property, if the allowed amount for offsite and demolition differs from HUD's estimate on Form HUD-92264 issued at Firm Commitment.

   b. Offsite costs are not allowable for leasehold estates when the ground rent is based on a land value that reflects all required offsite improvements since the borrower has not paid for those improvements.

   c. If the borrower certifies to off-site costs, the land value entered on Form HUD-92580, "Maximum Insurable Mortgage" will be reduced by the amount of off-site costs.

L. Other costs include all costs and/or recovery of costs which are not provided for elsewhere and which are clearly attributable to the actual cost of the project.

1. Cost of acquiring the leasehold interest provided the acquisition cost plus ground rent and offsite costs paid by the borrower, if any; do not exceed the HUD Fair Market Value of the Land Fully Improved. Any excess is to be reflected as a disallowed cost of acquiring the leasehold.
2. Ground rent paid during the period of the first mortgage between initial endorsement (start of construction for insurance upon completion projects) and the cut-off date as defined in Section 13.7.
3. Incentive payment due a nonidentity of interest contractor for completing construction before the scheduled completion date as amended by HUD-approved change orders.
4. Compensation from an insurance claim including any income earned by investing the proceeds of the claim. Treat as recovery of cost after computing BSPRA.
5. Contractor's bond premium if paid by the borrower. If the construction contract contained an amount for the bond premium, subtract it from the contract amount when developing the adjusted upset price on line 1c of Form HUD-92331A.
6. Other fees, including engineering and topographical survey. Cost staff must determine if such costs are reasonable and not duplicated in the general contractor's costs.
7. Contingency reserve is included in the replacement cost of substantial rehabilitation projects.

   a. The contingency reserve may be used for unforeseen costs of necessary change orders approved by HUD and unanticipated soft costs for time extensions approved by HUD.

   b. Expenditures for change orders and shortfalls in soft costs should be certified to and allowed under those specific line items.

   c. Normally there will not be an amount certified to under contingency reserve since all expenditures will be certified to on other line items.

   d. An itemization of all expenditures covered by contingency reserve funds must be attached to the cost certification submission.

8. Grants, governmental loans or tax credit equity used to pay for allowed cost items.
   a. Should be treated as a recovery of cost after BSPRA.
   b. Do not deduct grant, loan or tax credit equity funds from the total recognized costs when the funds were used to pay for the non-replacement cost items, i.e., used toward but not limited to: paying the acquisition cost of the land in excess of the HUD allowance, the operating deficit, working capital and items on Form HUD-2880, Applicant/Recipient Disclosure.
9. Residential relocation fund established on Form HUD-92264. Allow only those expenses approved by the HUD CPD relocation specialist up to the amount established on Form HUD-92264. Apply unused allowance as a direct mortgage reduction.
10. Third Party costs for appraisals, market analysis, PCNA etc., are no longer recorded in Other Fees and should be included with Organizational Cost line items (refer to Chapter 3).

M. BSPRA

1. HUD does not control the division of BSPRA.
2. Compute BSPRA without regard to amounts on Form HUD-92264 based on a percentage of allowed costs.
   a. Use the same percentage (not to exceed 10%) in the Firm Commitment review.
   b. Exclude from the computation the cost of off-site work, land, payments for acquisition of leasehold, ground-rent, relocation expenses, and supplemental management funds, and Major Moveable Equipment, if applicable.
3. 50/75% rule.
   a. Whether or not there is an identity of interest, <u>no</u> general contractor's fee (general overhead and profit) will be allowed when:
      (1) More than 50% of the contract sum in the Construction Contract–Cost Plus, Form HUD-92442M, is subcontracted to one subcontractor, material supplier or equipment lessor, or

      (2) 75% or more with three or less subcontractors, material suppliers and equipment lessors.

   <u>NOTE</u>: If two or more subcontractors have common ownership, they are considered as one subcontractor.

   b. Exceptions: The 50/75% rule is not applicable to:

      (1) Manufacturers of Industrialized Housing.

      (2) Trade items performed by persons on general contractor's payroll.

      (3) Supplemental Loan program.

(4) Rehabilitation programs other than substantial rehabilitation.

c. The cost analyst determines the applicability of the 50/75% rule.

d. Where the 50/75% rule is violated, the general contractor forfeits its profit and only Sponsor's Profit Risk Allowance (SPRA) is allowed.

4. Where there is no identity of interest between the borrower and builder or when the 50/75% rule has been violated, compute a SPRA which is 10% of allowable:

a. Architectural fees.

b. Carrying charges and financing.

c. Legal, organization, and audit expenses.

5. If an identity of interest between the borrower and general contractor is established after initial endorsement and exists at the time of substantial completion, BSPRA is allowed in lieu of a builder's profit and SPRA.

6. If prior to the substantial completion date an identity of interest no longer exists between the borrower and builder, substitute SPRA for BSPRA.

a. The construction contract may be amended to permit a typical builder's profit.

b. Treat the difference between BSPRA and the combination of SPRA and builder's profit as a direct mortgage reduction on Form HUD-92580.

N. Non-Profit Developer Fee. The allowable amount is included in the Firm Commitment less amounts certified and allowed on other line items.

13.17 Cost Review of Contractor's Cost Certification

A. Actual costs are all costs, paid by the general contractor under the Construction Contract for completion of the project, and to which the general contractor certifies, using Form HUD-92330A.

1. Include actual costs paid in cash, or to be paid in cash (such as items of delayed completion), within 45 days after the date of the substantial completion, for labor, materials, equipment, subcontract work, general requirements (job overhead), fees and general overhead. Also include amounts estimated for any items requiring an escrow.

a. General Requirements:

(1) May include salaries of clerical staff for time actually spent at the project site. Prorating of annual salaries on the percent basis is not permitted.

(2) Salaries of executives may not be included in General Requirements. Such salaries are included in General Overhead.

b. General Overhead:

(1) Include only the amount of the accepted Schedule of Values, Form HUD-2328, adjusted by the effect of approved change orders.

(2) Itemization is not required.

2. Kickbacks, rebates, adjustments, discounts, or any other devices which the contractor may have received or is entitled to, must be deducted from actual costs.

B. For those cases where the borrower is not seeking a mortgage increase or a detailed review is not requested by the Hub Director:

1. The cost analyst will not review Form HUD-92330A, Contractor's Certificate of Actual Cost, in assisting the Mortgage Credit Examiner in the analysis of the Borrower's cost certification.
2. The cost analyst will advise Mortgage Credit Examiner of the approved change orders.

C. Cost Review

1. Conduct a detailed review when the borrower applies for a mortgage increase or the Hub Director orders a detailed review.
2. Review certifications where required from the contractor, or any subcontractor, equipment lessor, material supplier or manufacturer of industrialized housing.
3. Forms necessary to make reviews:
   a. Form HUD-92330, Borrower's Certificate of Actual Cost.
   b. Form HUD-92330-A, Contractor's Certificate of Actual Cost.
   c. Form HUD-93305M, Agreement and Certification.
   d. Form HUD-92437, Request for Construction Changes–Project Mortgages.
   e. Form HUD-92326, Project Cost Estimate (HUD Estimate).
   f. Form HUD-2328, Contractor's and/or Borrower's Cost Breakdown.
   g. Form HUD-92331-B, Cost Certification Review Worksheet.
   h. Form HUD-92331, Summary of Cost Certification Review.
   i. Form HUD-95379, Trip Report.
4. Steps to conduct the review:
   a. 50/75% rule check. Use information from the "total" and "name of subcontractor or payee" columns of the general contractor's cost certification. If the rule applies, disallow the general contractor's general overhead and profit. If the project uses BSPRA, disallow only the general overhead and inform the Mortgage Credit Examiner.
   b. Identity of interest subcontract review (for Borrower, general contractor, subcontractors, equipment lessor, material suppliers, and industrialized housing manufacturers):

      (1) Examine Form HUD-93305M and Form HUD-92330-A to establish all declared identities of interest.

      (2) Review each identity of interest subcontractor's cost certification.

NOTE: If cost certification not received, disallow subcontractor's overhead, profit, and all questionable costs.

(a) If no prior approval as an identity of interest subcontractor, disallow subcontract overhead and profit.

(b) For prior approval:

(i) Allow prior approved subcontract overhead and profit, plus or minus the effect of approved change orders. Disallow excess.

NOTE: Do not reduce the prior approved subcontract overhead and profit in the event that the certified cost for the work is less than the prior approved maximum subcontract price.

(ii) Allow up to the prior approved maximum subcontract amount for work, plus or minus the effect of approved change orders. Disallow excess.

5. Trade line item review:

a. On Form HUD-92331-B

(1) Enter all trade line costs from HUD estimate (Form HUD-92326) or Contractor's schedule of values (Form HUD-2328) after adjusting for approved change orders.

(2) Enter all trade line costs from general contractor's cost certification (Form HUD-92330-A). Take architect's fees from borrower's cost certification (Form HUD-92330).

(3) Using dollar and percentage variance columns compare each trade's actual cost with the estimate. Determine allowable amounts.

b. Allowable amounts are not limited by the estimates. Analyze differences.

(1) Allow actual costs paid to complete the work in accordance with the construction contract.

(2) Allow actual costs due to unusual circumstances, e.g., subcontractor bankruptcy, code changes, required replacement of completed work, replacements due to natural occurrences (storms, floods, earthquakes, etc.).

c. Question only amounts substantially in excess.

(1) Contact general contractor and/or borrower requesting explanation or more documentation.

(2) Make disallowances if explanation/documentation is not received in a reasonable amount of time.

(3) Only the accountant may make reallocation of monies from one trade item to another.

(4) As a result of discussion, have the accountant amend Form HUD-92330-A and resubmit.

d. Disallow any amount not justified or supported as being part of the construction contract work.

e. Disallow costs for duplication of work due to contractor's error or negligence, e.g., improper placement, failure to protect, noncompliance with contract, etc.

D. Summary of Cost Certification Review on Form HUD-92331

1. Enter all recommended disallowances.
2. Enter summary of construction contract costs.
3. Enter contractor's profit from borrower's Form HUD-92330. Add profit from all HUD approved change orders.
4. Enter offsite costs from borrower's Form HUD-92330, if applicable.
   a. Review itemized offsite breakdown.
   b. Disallow any cost duplication on general contractor's Form HUD-92330-A.
5. Property Insurance Schedule, Form HUD-92329. Complete new form using allowed construction costs.

E. Lump Sum Construction Contract Cost Certification

1. Review borrower's certification (Form HUD-92330) if requested to do so by Hub Director.
2. Review cost certification of any subcontractor that has identity of interest with the borrower.

13.18 Determination of the Nonprofit Borrower's Initial Equity Investment

The nonprofit borrower under the Section 221(d)(3) will be permitted a 6% return on its initial equity as computed on Form HUD-92580, Maximum Insurable Mortgage.

A. The base equity is determined as follows:

1. New Construction: Line 6, Form HUD-92580, minus finally endorsed mortgage determined in line 10 of the form.
2. Rehabilitation–Property Owned: Reduce the sum of line 4, Form HUD-92580, plus HUD's estimate of the "as is value" of the existing land and improvements before rehabilitation, by the finally endorsed mortgage determined in line 10 of the form.
3. Rehabilitation–Property Acquired: Reduce the sum of line 4, Form HUD-92580, plus the lesser of HUD's estimate of the "as-is value" of the existing land and improvements before rehabilitation or the acquisition cost of the property, by the finally endorsed mortgage determined in line 10 of the form.
4. Rehabilitation under Section 220 and 221(d): Use the New Construction formula in paragraph A.1 above.

B. The base equity computed in paragraph A.1 above may be increased by:

1. The cost of furnishing, equipment or other betterments essential to the operation of the project.
2. The nonprofit developer's fee used to reduce the estimate closing costs of the project.
3. Grants from national, regional, and local community service organizations (non-government source).
4. Sponsor's cash contribution for the cost of land over and above what HUD has allowed.

C. Modify the Regulatory Agreement to require the return on equity be used for:

1. Continued affordable housing initiatives; or
2. Pledged to the repayment of surplus cash or residual receipts notes held as secondary financing.

D. Asset Management will monitor the nonprofit borrowers to be certain that the return on equity is used only for permissible purposes.

E. The return on equity is paid from surplus cash/residual receipts. Any shortfall in the permitted return in one year may be made up from surplus project funds in a future year.

13.19 Determine the Borrower's Initial Investment

A. New construction and substantial rehabilitation projects under Sections 220 and 221(d): Line 6, Form HUD-92580, minus the maximum insurable mortgage determined in line 10 of this form.

B. The amount determined by above Paragraphs A may be increased by:

1. Expended working capital funds not recognized in the cost certification review.
5. Residential relocation expenses approved by the relocation specialist in excess of the amount established on Form HUD-92264, Section G, and Section O, Remarks and Conclusions.

C. Distributions. Mortgagor or any Affiliate or Principal shall not make, receive or retain any distribution of assets or any income of any kind from the project, except from Surplus Cash (per the Regulatory Agreement, Form HUD-92466M).

13.20 Section 223(f) Modified Form of Cost Certification

A. Complete and submit a modified form of cost certification for review 15 days before the initial/final endorsement of the loan for insurance for all projects processed pursuant to Section 223(f); except those 207/223(f) refinancing transactions where 75% or less of value is the

controlling criterion. (In such case cost certification is not required.) Unlike other cost certification procedures, savings from one line item cannot offset cost overruns on another line item. As you complete the cost certification and there is a cost savings, you must recalculate the maximum insurable mortgage. Refer to Form HUD-2205-A's instructions.

1. The borrower must certify to the total actual costs incurred in the acquisition or refinancing of the property. The certification must be submitted on Form HUD-2205-A, and it must be dated and signed by an authorized agent of the borrower.
2. The mortgagee must submit the certification to HUD for computation of the maximum insurable mortgage and completion of Section II of Form HUD-2205-A.
3. If, in a purchase transaction, the amount of the acquisition cost determined allowable at cost certification exceeds the estimate of value, which was determined during processing, the rent formula shall be recomputed. This re-computation may be accomplished using the allowable acquisition cost as determined by cost certification and the dollar amount of secondary financing represented by the approved promissory notes (Form HUD-92223).

B. The borrower must submit a supplemental cost certification where an escrow was established at initial/final endorsement to complete non-critical repairs. In cases where the actual costs are less than estimated, you must recalculate the maximum insurable mortgage. If the maximum insurable mortgage is reduced because of the lower actual costs, the borrower must either:

1. Provide the required prepayment to the mortgagee, or
2. Have the required prepayment deducted from the repair escrow.

13.21 Mortgage Reduction after Cost Certification

A. The National Housing Act requires that the mortgage will not exceed the applicable percentage of actual costs. If certified actual costs are lower than original projected cost as reflected in Form HUD-92264, a reduction in mortgage may be applicable. The Agreement and Certification, Form HUD-93305M, also addresses this issue and provides that where the HUD accepts, for cost certification, estimates of cost for any item, the later substitution of certified actual costs may require a reduction of the mortgage.

B. Reductions of cost may arise from:

1. Refunds, rebates, or discounts.
2. Excess of escrows over the actual costs of incomplete construction items.
3. Refunds of deposits made by the borrower to prevent losses to the mortgagee from loss in connection with sale of the mortgage.
4. Settlement of claims against bonding companies or others after project completion.

C. At final endorsement, the borrower must set up a cash escrow to pay all "to be paid in cash items" identified on Form HUD-92330, Borrower's Certificate of Actual Cost, and debts to third parties who made the original disbursement for an item listed as paid on Form HUD-92330.

1. Reconcile the difference between:

   a. Obligations listed on Form HUD-92023M, Request for Final Endorsement of Credit Instrument or HUD-92455M (for Insurance Upon Completion Projects only), and

   b. The "to be paid" column on Form HUD-92330 plus debts to third parties.

2. Paid receipts must support differences and a statement from the borrower identifying by name and cost, those items paid in cash. The receipts and statement are affixed to Forms HUD-92023M or HUD-92455M.

3. Do not accept personal or business checks issued by the borrower at final endorsement as evidence of payment. Payment must be in certified or cashier checks.

4. Prepare a new Form HUD-92331A to disallow obligations listed as "paid" or "to be paid" on Form HUD-92330, which are represented at final endorsement as paid by HUD-approved notes. Prepare a new Form HUD-92580 from the total of HUD-approved cost of revised Form HUD-92331A.

5. Undisbursed mortgage proceeds may supplement or satisfy the cash escrow.

6. Use Form HUD-92476.1M, Escrow Agreement for Non-Critical, Deferred Repairs (formally Escrow Agreement for Unpaid Construction Costs):

   a. To set up the cash escrow.

   b. Attach a detailed listing of the unpaid costs.

7. Use Form HUD-92464M, Request for Approval of Advances of Escrow Funds to disburse escrow.

8. Escrow should be disbursed within 45 days after final endorsement. If all of the funds are not disbursed follow the procedures in Section D below.

9. At final endorsement, if all obligations have been paid in cash, nothing else is needed.

D. Sixty-days after final endorsement:

1. Prepare a new Form HUD-92331A. Enter under the column heading:

   a. "92264" - the amount of each item of cost recognized from the earlier Form HUD-92331A "Allowed" column.

   b. "92330/92330A" - the amount listed in Column C of the Borrower's Certificate of Actual Cost, Form HUD-92330, for each item of cost.

   c. "Allowed" - the amounts paid in cash based on the reconciliation performed in Section B above and disbursements from the cash escrow account.

   c. "Disallowed" - the lower of the amounts previously allowed or paid in cash.

2. Compute a new Maximum Insurable Mortgage, Form HUD-92580, based on the total of the "Disallowed Column" (Form HUD-92331-A). If this computation produces an amount less than the mortgage finally endorsed:
   a. Notify the Directors of Housing Development and Management by memorandum that prepayment to the mortgage is required.
   b. Prepayment is mandatory and is applied:
      (1) In amounts equal to the scheduled monthly principal payments, to the extent possible.
      (2) Any remainder goes to the Reserve for Replacements Fund.
   c. If HUD is notified that payment has been delayed because of a dispute or litigation, retain funds to pay the amount pending resolution of the dispute.
   d. Notify the mortgagee or escrow agent by letter of the required prepayment.
   e. Control the remaining balance in a special account, as a reserve for unpaid construction costs from which disbursements may be made only after written consent of the Hub/PC.
3. The mortgagee will continue to use the existing amortization schedule for servicing the mortgage.
   a. The prepayment is in addition to the regular monthly payments to principal.
   b. There is no adjustment in the amount of the annual MIP due because of these mandatory prepayments.
4. The escrow requirement does not apply to funds the general contractor owes. However, the general contractor must submit a reconciliation of its "to be paid" items.

13.22 Increase in Mortgage Amount

A. Timing. Requests for a mortgage increase will not be considered until the project is complete, cost certification has been submitted, and the Final Endorsement will likely be achieved immediately following processing of the mortgage increase and the conditions in paragraph B below are met.

B. Bases for considering a mortgage increase:
   1. Necessary changes that arise from differing site conditions (as defined in the construction contract).
   2. Compliance with local codes.
   3. Unforeseen conditions that might affect the safety and health of occupants.
   4. Betterment changes that are economically justified e.g., those that produce significant cost savings to project operation can be reflected in increased income expectancy, or enhance the security of the mortgage.

C. Costs caused by extensions in construction time, when such extensions: are approved by HUD; justifiable under AIA General Conditions; and caused by problems beyond the contractor's control.

D. Other costs not known at Firm Commitment resulting from requirements of local authorities and beyond the borrower's control.

E. Construction hard cost increases caused by a natural disaster declared by Federal or State government, to the extent not covered by casualty insurance.

F. Increased costs resulting from concealed subsurface site conditions, provided it is determined those exploratory tests during project design were sufficient and thorough and neither the architect nor engineer was at fault.

G. Cost of substituting a general contractor when the original general contractor is terminated for cause and the surety has failed to perform.

H. To correct a substantial HUD error in the original processing that would otherwise result in serious inequities.

I. Any mortgage increase for an insured project must be more than 2.5% of the original mortgage and at least $50,000.

13.23 Restrictions on Mortgage Increases

A. A mortgage increase may not be granted for cost overruns associated with: completion of the work in accordance with the original contract documents by the original contractor, changes made primarily for the convenience of the borrower or contractor, nor for the aggrandizement of the borrower or contractor.

B. Cost overruns are not a basis for granting a borrower's request for mortgage increase nor are changes made primarily for the convenience or aggrandizement of the borrower or contractor.

C. Any mortgage increase for an insured project must be more than 2.5% of the original mortgage and at least $50,000.

D. The increase must be supported by net income under Criterion 5 of Form HUD-92264-A.

E. A mortgage increase may not be granted for replacing a contractor where the borrower sets up a "straw contractor" for purposes of BSPRA.

13.24 Processing a Mortgage Increase

Technical processing consists of Step One through Step Four below. The four steps to processing a mortgage increase, depending on the condition being considered:

A. Step One: Use the alternative applicable to the condition being considered:

1. Alternative One, applicable to necessary and betterment change order cost increases:

   a. Architecture and Valuation staffs review the change orders to determine eligibility for processing a mortgage increase. Architecture further reviews for the added cost.

   b. Mortgage Credit computes the allowable costs on Form HUD-92331-A, Cost Certification Review Worksheet–Mortgage Credit Staff, Line 1.d. Reduce this amount by the cost attributable to any change order(s) not qualifying for a mortgage increase.

   c. The adjusted hard cost forms the basis of the mortgage increase computation

2. Alternative Two, applicable to contract time extension soft cost increases:

   a. Mortgage Credit computes the allowable costs on Form HUD-92331-A, Cost Certification Review Worksheet–Mortgage Credit Staff, Line 3 through 6.

   b. The adjusted soft cost forms the basis of the mortgage increase computation.

3. Alternative Three, applicable to construction contract cost increases due to a change in the contractor:

   a. A&E staff computes a new Form HUD-2328 and Form HUD-92264, Section G through Line 50.

   b. Mortgage Credit staff computes the allowable costs of Form HUD-92331-A, Cost Certification Review Worksheet–Mortgage Credit Staff, Line 1.c. for hard cost increases between the original contractor and the contractor completing the work, and Lines 3 through 6 for soft cost increases associated with the change in contractor.

   c. The adjusted hard and soft costs form the basis of the mortgage increase computation.

4. Alternative Four, applicable to substantial error in HUD cost processing:

   a. A and E staff computes a new Form HUD-2328, and Form HUD-92264, Section G through line 50.

   b. Mortgage Credit computes the allowable costs on Form HUD-92231-A, Cost Certification Review Worksheet–Mortgage Credit Staff, Line 1.c, using the criteria in paragraph c. below.

   c. The allowable construction costs for processing the increase will be based upon the lesser of:

      (1) The amount of the construction cost certified by the borrower, or

      (2) The upset price of the construction contract as adjusted by approved change orders eligible for a mortgage increase, plus the increases resulting from correcting or errors in the original processing.

   d. The adjusted hard cost forms the basis of the mortgage increase computation.

NOTE: The mortgage credit examiner must not use the adjusted upset price of the construction contract as a limiting criterion at cost certification where there is a substantial error in HUD cost processing.

B. Step Two: Mortgage Credit must compute (for use by Valuation in completing Form HUD-92264) the eligible costs and fees for the following: architect's fees, bond premium if paid by the borrower, other fees not included in the construction contract and paid by the borrower, interest, taxes, insurance, developer's fee (if applicable), legal, organizational and audit fees, marketing (if applicable), offsite costs, as-is land value and "as-is" value of property (if applicable). Mortgage credit must comply with the following in computing the costs and fees.

1. Do not increase BSPRA or restore Contingency Reserve or nonprofit's Developer's Fee.
2. Do not include non-mortgageable items (construction or permanent loan extension fees; discount rate, maintenance fees, etc.)
3. Offset non-mortgageable items by net income (net non-proprietary income, if applicable) to offset amount of mortgage increase, and
4. For increases caused by natural disaster:
   a. Consider in the revised cost any increases from any interim closing for: carrying charges, financing fees, and legal fees. Do not include any cost due to construction delays before the disaster,
   b. Cut the new estimated replacement cost by the amount of any actual recovery through insurance proceeds, and
   c. Require prepayments to be made for any late recovery of insurance proceeds.

C. Step Three. Valuation must use the costs and fees developed by Mortgage Credit in Step Two in revising Form HUD-92264. Valuation must consider each of the following:

1. Examination fee, initial service fee, GNMA fee, inspection fee, MIP, and title and recording based on the approvable increased mortgage amount.
2. Net income derived from market rent, expense and occupancy estimates current as of the date of mortgage increase processing.

D. Step Four. Mortgage Credit must prepare a revised Form HUD-92264-A, using the revised Form HUD-92264 and Trial Form HUD-92264-A prepared by Valuation in Step Three.

13.25 Authorization to Reopen Mortgage Transaction

A. The Lender must advise the mortgagee of HUD's approval or denial of the request for a mortgage increase upon completion of technical processing. Use Specimen Letter–Agreement Authorizing Reopening of Mortgage Transaction (Appendix 14A), to notify the mortgagee, where a determination is made to increase the mortgage.

1. Approval of a mortgage increase is subject to the payment of the following fees based on the amount of the increase.
   a. Application Fee of $3.00 per thousand of the increase.
   b. Inspection Fee of $5.00 per thousand of the increase is applicable only when the increase involves construction hard costs.

13.26 Deferment of Principal Payments

The Lender must obtain an agreement from the investor in the GNMA security and support the request for deferment of principal payments.

A. HUD may consider requests for deferment if:
   1. There is a delay in construction; or
   2. The project requires additional time to reach sustaining occupancy.

B. HUD may approve the request when:
   1. There are sufficient funds outside the mortgage proceeds for payment of interest overrun as confirmed either:
      a. Written assurance from the sponsor, or
      b. Exercise of action against the contractor.
   2. The borrower shows reasonable effort to complete construction and attain sustaining occupancy.

C. The period of deferment is the additional time necessary for the borrower to stabilize its operation.

D. Deferment Letter. Use Appendix 14B, Specimen Letter – Agreement Authorizing Deferment of Principal Payments for Level Annuity Monthly Payment, and distribute copies in accordance with Section 13.27 below.

E. Deferment Instruments. The Hub Director is authorized to approve modifications of the mortgagee instruments as may be necessary to effect the deferment of principal payments. The HUD closing attorney must clear the instruments.

13.27 Document Distribution

A. Form HUD-92580, Maximum Insurable Mortgage.
   1. Mortgagee–original and one executed copy.
   2. One executed copy to each of the following: Closing Attorney, Mortgage Credit Control File, Washington Docket, Hub/PC Docket, Hub/PC Valuation Data Bank.

B. Cost Certification Documents. Original documents filed in the Washington Docket and one copy in the Hub/PC Docket.

13.28 Office of Inspector General

The Hub Director should refer borrowers to the Office of Inspector General to evaulate the borrower's and/or contractor's books where discrepancies appear to arise from other than inadvertent error, or creditable misinterpretation of applicable criteria. Do not issue Form HUD-92580, Maximum Insurable Mortgage, before completion of an OIG audit or investigation initiated before its issuance. A referral must also be requested for any indicated fraud or material misrepresentation detected after issuance of Form HUD-92580.

13.29 Cost Certification Incontestability

After HUD approves the certifications and issues Form HUD-92580, Maximum Insurable Mortgage, they are final and incontestable unless there is fraud or material misrepresentation by the borrower, general contractor, or subcontractors.

13.30 Post Closing Escrows

Post Closing Escrows must be set up at final closing to pay all "to be paid in cash" items identified on Form HUD-92330, Borrower's Certificate of Actual Cost, and debts to third parties who made the original disbursement for an item listed as paid on Form HUD-92330. These amounts may be adjusted for payments made between the cut-off date and the date of final closing.

Chapter 14

LIHTC and other Tax Credit Program Guidance

14.1 Introduction

The Low Income Housing Tax Credit (LIHTC) program was enacted as part of the Tax Reform Act of 1986 and is administered by the Treasury Department and the State Housing Finance Agencies (HFA). In July 2008, the Housing and Economic Recovery Act (HERA) was enacted which made changes to the FHA multifamily programs to facilitate the use of insured mortgages with LIHTC developments.

The Guide and this chapter outline the policies and procedures to follow when underwriting and reviewing all insurance applications referenced under Title II of the National Housing Act with tax credits. Standard processing of applications apply except as modified below.

14.2 Affordable Housing Underwriting and Program Guidance

Most of the guidance for processing and underwriting insured loans for affordable housing projects under the mortgage insurance programs can be found in earlier chapters of this Guide, as follows:

Section 2.6	Identity of interest permitted between Lender and tax credit equity syndicator, investor or bridge loan Lender, in limited circumstances
Section 3.2 & 4.2	No pre-application fees on affordable projects under Section 221(d)
Section 3.2	Definition of affordable housing
Section 3.5	Loan sizing ratios under 221(d)(4)
Section 3.6	Loan sizing ratios under 221(d)(3)
Section 3.7	Loan sizing ratios under 220
Section 3.8	Loan sizing ratios under 231
Section 3.9	Loan sizing ratios under 223(f)
Section 4.1	One stage application processing permitted under Section 221(d)
Section 5.28	Delayed submission of final plans permitted for tax credit projects
Section 7.4	No market study required if 90% or more rental assistance

Section 7.5	Requirements for market studies
Section 7.9	Estimating the land value
Section 7.14	Calculating operating deficits
Section 7.16	Recognizing tax abatements in the underwriting
Section 7.17	Estimating the completed affordable project value
Section 8.3	Indentifying the principals in a LLC, LP or non-profit for mortgage credit review; limited review of tax credit equity syndicators and passive investors
Section 8.4	Financial requirements of sponsors of affordable projects
Section 8.7 & 8.8	Determining the mortgage amount and cash requirements; no escrowing of tax credit equity during construction; Firm Commitment special conditions for deferred equity pay ins.
Section 8.9	Requirements for secondary financing from governmental Lenders and for equity bridge loans; use of HUD form Subordination Agreement instead of Note Rider
Section 8.10	Requirements for grants and loans from governmental sources
Section 8.11	Evaluating mortgage credit of nonprofit sponsors
Section 8.13	Cash requirements for tax credit projects, including working capital and operating deficit escrows
Section 8.14	Requirements for tax exempt bond financing
Section 13.4	No cost certification required for tax credit loans under 80% of cost
Section 16	Requirements for master leases on tax credit projects

14.3 Subsidy Layering Review

HUD's Subsidy Layering Review requirement have been eliminated for LIHTC projects with mortgages insured under Title II of the National Housing Act and which have other sources of federal subsidy, so most of HUD's mortgage insurance programs are exempt. HFA or GSE risk-sharing mortgages still require Subsidy Layering Review.

14.4 Historic Rehabilitation and New Markets Tax Credits

All provisions of the Guide applicable to LIHTC are also applicable to Historic and New Markets tax credit equity projects.

14.5 Build America Bonds

A. Build America Bonds (BABs): BABs are an alternative to financing government sponsored projects using tax exempt bonds. BABs are taxable bonds for which the US Treasury will rebate 35% of the interest paid, thus making the taxable rate effectively a tax exempt rate. BABs can only be used for projects owned by public agencies, such as those sponsored by Public Housing Authorities (PHA). FHA will insure mortgages to fund BAB projects under the applicable insurance programs.

B. Applicable Insurance Programs: New construction or substantial rehabilitation projects that use BABs are not eligible for processing under the 221D(3) program and should only be processed under 221D(4). BABs can be used for urban renewal projects processed under Sec 220 or for refinancing under 223(f), assuming compliance with all MAP underwriting guidance on BABs and on the applicable insurance program.

C. Underwriting: BAB bonds do not impose affordable rent or occupancy restrictions and many BAB projects are for market rate housing. Appropriate DSC, LTV, LTC, IOD, working capital and maximum occupancy standards and unit absorption periods should be imposed in accordance with program requirements. The Lender may or may not elect to recognize the BAB interest rebate in the underwriting. If it is not recognized, the rebate will be outside of the insured transaction, will not be subject to the FHA loan documents and will simply represent extra income to the PHA. When sizing the loan, the Lender should: a) use a loan constant based on the full taxable bond rate, and, b) if applicable, include the annual level interest rebate amount in project income.

D. Interest Rebate and Lag Fund: Since the amount of the rebate will decline each year as less interest and more principal is paid over the loan term, the stream of unequal rebate payments must be averaged to match the level loan payments due over the 35 or 40 year insured loan term. Thus, a portion of the higher rebates in the early years must be escrowed and applied to later years (similar to an uneven IRP stream in a de-coupled Section 236 project). The amount to be recognized in underwriting is the average monthly rebate payment. Since the entire interest payment due on the BAB bond must be made before the 35% rebate is received from Treasury, a Lender controlled rebate reserve must be established to act as a lag fund to bridge these rebate timing issues and to level the unequal rebate payments. The rebate reserve must be prefunded in an amount equal to the interest rebates to be received during the first 6 months of the permanent loan term. Any interest earned on the rebate fund will accrue to the account and may not be recognized in the loan underwriting. The Lender may charge a fee for administering the rebate fund. A vacancy rate on the rebate income is not required, aside from the vacancy applied to the project physical occupancy. The construction period interest account should be sized sufficient to carry the insured BAB loan until Final Endorsement with accrual of all rebate income during that time.

E. Project Ownership: Because a BAB project must be owned only by a governmental agency, FHA must be sure that the PHA or another governmental agency will always remain the owner. Thus, a PHA that proposes a BAB transaction must form a single asset entity structured with 99% of the

GP interest held by the PHA and 1% held by another governmental agency, preferably the state HFA, because it has asset management capacity, is not a line agency of the state or city government, and has its own sources of revenue. In this way, the HFA could assume ownership of the GP interest if the PHA should withdraw or fail. If the state HFA is not willing to participate in the ownership of a BAB project, the Lender should discuss other available options with the Hub/PC.

F. Permitted Bond Structures: By recognizing the interest rebate in project income, most BAB mortgages will be cost or value constrained and will generate excess distributable surplus cash. To capitalize on this excess cash flow, some BAB transactions may be structured with an A/B bond structure. If there is a B bond, it must be a non-asset bond that is: a) not FHA insured or securitized by GNMA, b) not secured by a subordinate lien on the real estate, and c) if the rebate had been recognized in underwriting the project income, payments on the B bond will be subject to available distributable surplus cash after payment of all project operating expenses and approval of distributions by HUD.

G. BABs and Exchange Funds: Some BAB transactions may also plan to use exchange funds. It is not clear if BAB projects qualify for exchange since to do so, they would otherwise have to qualify for LIHTC which raises issues about the form of ownership (LIHTC projects must be owned by a for profit entity and BABs must be owned by a public agency) and the compatibility of BAB bonds with exchange funds (since BABs are taxable bonds with an interest rebate that makes them effectively tax exempt, and tax exempt bonds are not eligible for exchange). Before proceeding with any BAB transaction that proposes to use exchange funds, the Lender should obtain an opinion from borrower's counsel that combining these resources is legally permitted and should confirm that directly with the state agency that allocates the exchange funds.

14.6 TCAP and Exchange Funds

A. TCAP funds were made available to affordable projects by state housing agencies as soft secondary loans to fill gaps in the project financing due to the reduced equity value of selling tax credits. All funding available under TCAP has been committed to qualifying projects. A project may use both TCAP and Section 1602 exchange funds. A Lender underwriting a TCAP loan should follow the requirements for secondary financing from a governmental source in Sections 8.9 and 8.10. State agencies which administer TCAP funds have varying loan terms and requirements. HUD has reached agreement with most states on an acceptable form of subordination agreement applicable to TCAP secondary liens. Contact the property Hub or PC for instructions and sample forms.

B. IRS Section 1602 exchange funds are allocated to LIHTC projects by state housing agencies as a substitute for, or as a supplement to, tax credit equity investment from a syndicator or investor. All funding available under the Section 1602 exchange program has been committed to qualifying projects. Exchange funds can be made available to a project as a grant or as a subordinate lien. Exchange funds should be viewed as equivalent to LIHTC equity and the same requirements applicable to LIHTC projects apply, such as limits on the amount of equity that must be funded at closing and prohibition on escrowing the balance. State agencies which administer exchange funds have varying terms and requirements. If the exchange funds are to

be secured by a subordinate lien, HUD has reached agreement with most states on an acceptable form of subordination agreement or note rider applicable to exchange subordinate liens. Contact the property Hub or PC for instructions and sample forms.

The following criteria are to be applied to exchange fund transactions which are not grants. Exchange funds: a) can be secured by a lien on the property only if it is subordinate to all other liens and only if the exchange Lender enters into an acceptable form of subordination agreement or note rider with HUD; b) no monthly or annual repayment of the exchange note may be required, no interest may be due or may accrue on the exchange note; c) in the event of a default on the FHA mortgage, the exchange lien holder must stand still and may not exercise any remedies as against the property or the sponsor; d) the exchange loan may have a maximum 15 year term, each year during the term, 1/15th of the exchange loan must be forgiven, and in year 15, the exchange lien must be released and the exchange note must be discharged with no repayment of principal due; and e) violation of the LIHTC regulatory agreement may be the only event of default under the exchange note and the only remedy for the exchange note holder is to seek recapture from the property's general partner (GP). These criteria will not affect the enforceability of Extend Use Agreements (EUA) or Land Use Restrictive Agreements (LURA) imposed by the states that may be in effect beyond year 15.

14.7 LIHTC Coordinators

The HQ Office of Multifamily Development has established a lead LIHTC Coordinator and each Hub or PC has a designated field LIHTC Coordinator. Below is the objective of the LIHTC Coordinators.

Role of the designated LIHTC Coordinator:

1. Enhance staff knowledge of the LIHTC program;
2. Expedite and coordinate the processing of FHA insurance applications with LIHTCs;
3. Perform outreach of FHA's mortgage insurance programs to industry partners;
4. Act as local contact person regarding FHA insurance programs and LIHTC issues;
5. Increase processing consistency among Hub/PC offices; and,
6. Communicate with HQ regarding local issues or proposed changes to state policy/procedures involving LIHTCs and the insurance programs).

NOTE: It is expected that the content contained in this chapter will be replaced by a new regulation adopted by the Department to implement and govern a Multifamily Credit Watch monitoring, violation scoring and enforcement system, which is expected to be adopted later this calendar year after public notice and comment.

Chapter 15

Quality Assurance Enforcement Actions

15.1 Oversight of Map Lenders

By permitting a MAP Lender to prepare much of the documentation for a loan submission for mortgage insurance, HUD places confidence in the Lender's integrity and competence. HUD and MAP Lenders have a mutual interest in ensuring consistent Lender competence and compliance with the MAP Guide and other relevant guidance and handbooks. If in the process of performing this work, the Lender places HUD at un-due risk, HUD will issue a Warning Letter or sanction the Lender.

Every HUD multifamily employee plays an important role in the MAP Quality Assurance (QA) effort. This Chapter provides QA guidance to Program Centers, Hubs, and the Office of Multifamily Development (OMD) Headquarters, including the Lender Qualifications and Monitoring Division (LQMD). Such quality assurance tools are: i) Warning Letters; ii) Probation; iii) Suspension; iv) Termination; v) Limited Denial of Participation (LDP); and vi) referral to the Mortgagee Review Board or the Office of Inspector General. An LDP is a sanction applied to participants in loan transactions other than FHA-insured Lenders under procedures set forth in 2 CFR § 2424 Subpart J. The purpose and authority of the Mortgagee Review Board is set forth in 24 CFR Part 25.

15.2 Authority to Issue MAP Sanctions

A. General.

1. At any time, a Hub/PC Director or the Director of the Office of Multifamily Housing Development (OMD) Headquarters may initiate discussions with a MAP Lender regarding any concerns HUD has with respect to any of the Lender's actions or personnel, or any changes the Lender should make in using its MAP authority.
2. If there are concerns about the Lender's underwriting and/or construction loan administration, a Hub/PC Director, or the Director of OMD may take certain actions detailed below.
3. Every HUD multifamily employee must refer any possible instances of fraud, material misrepresentation or other criminal violations to the Office of the Inspector General.

B. A Program Center Director may:

1. Recommend to the Hub Director that s/he recommend to the Director of OMD the Suspension or Termination of a MAP Lender.
2. Initiate the issuance of a LDP of an individual or a firm involved in a "covered transaction" as defined in 2 CFR 2424.220.

C. A Hub Director may:

1. Recommend to the Director of OMD the issuance of an LDP to an individual or firm involved in a "covered transaction" as defined in 2 CFR 2424.220.
2. Recommend to the Director of OMD that the MAP Lender be referred to the MAP Lender Review Board for possible Probation, Suspension or Termination.

D. The Director of OMD may:

1. Refer an individual or a firm involved in a "covered transaction," as defined in 2 CFR 2424.220 to Headquarters' Deputy Assistant Secretary (DAS) for Multifamily Housing for imposition of an LDP, which may be imposed nationwide or on a more geographically restricted basis.
2. Refer the MAP Lender to the MAP Lender Review Board for possible Probation, Suspension or Termination.
3. Issue a Warning letter.

E. The DAS for the Office of Multifamily Housing Programs may:

1. Issue a Warning Letter.
2. Place the Lender on Probation.
3. Issue a Suspension.
4. Issue a Termination letter.
5. Issue a Limited Denial of Participation.
6. Referral to the MAP Lender Review Board.
7. Referral to the Office of Inspector General.

F. All recommendations authorized in Sections 15.2B through E shall be in writing, and shall state the reasons for the recommendations and the supporting facts. Recommendations for an enforcement action shall be transmitted to the next higher level of review, as set forth above, together with copies of all supporting documents.

15.3 Basis for issuing a Warning Letter or Sanctioning a MAP Lender

A MAP Lender's improper, inaccurate or inadequate underwriting and construction loan administration may lead to a Warning Letter or other sanction from HUD. Examples include, ***but are not limited to,*** the following:

A. Minor offenses that may be the basis for a Warning Letter include:

1. Failure to provide required exhibits or the submission of incomplete or inaccurate exhibits. Although the MAP Lender will be permitted to correct minor errors or provide additional information, substantial inaccuracies or lack of significant information will result in return of the application and retention of any fees collected.
2. Repeated failure to complete processing to Firm Commitment unrelated to the project underwriting analysis.
3. Preparation of an underwriting Narrative Summary that is not supported by the appropriate documentation and analysis.
4. Failure to notify the HUD processing office promptly of changes in the mortgage loan application for a Firm Commitment that has been submitted, such as changes in rents, numbers of units or gross project area.
5. Failure to meet MAP closing requirements or construction loan administration requirements.
6. Business practices that do not conform to those generally adopted by prudent Lenders or that show irresponsibility.
7. Failure to cooperate with a LQMD review.

B. Serious offenses that might be the basis for a Warning Letter and/or Probation include:

1. Receipt of multiple Warning Letters over any one-year period. In determining which sanctions to pursue as a result of prior warning letters, HUD will consider the circumstances surrounding those warning letters and any corrective actions undertaken by the Lender.
2. Fraud or material misrepresentation in the Lender's participation in FHA multifamily programs.
3. Lender collusion with or influence upon third party contractors to modify reports prepared by the contractor that affect the contractor's independent evaluation.
4. A violation of MAP procedures by a third party contractor, which the MAP Lender knew, or should have known, was occurring and which, if performed by the MAP Lender itself, would constitute a ground for a sanction under this chapter.
5. Evidence that a Lender's improper, inadequate or inaccurate underwriting was a cause for assignment of an insured mortgage.
6. Identity-of-interest violations under Section 2.6.
7. Payment by or receipt of a payment by a MAP Lender of any kickback or other consideration, directly or indirectly from the sponsor or from any other participant in the transaction, which would affect the Lender's independent evaluation, or represent a conflict of interest, in connection with any insured mortgage transaction.
8. Failure to comply with any agreement, certification, undertaking, or condition of approval listed in a MAP Lender's application for approval.

9. Noncompliance with any requirement or directive of the Director of OMD.
10. Violation of the requirements of any contract with HUD or violation of the requirements in any statute, regulation, handbook, notice, mortgagee letter, or other written rule or instruction including the MAP Guide as interpreted by answers to Frequently Asked Questions (FAQ's) that are posted on the MAP website.
11. Submission of false information or a false certification to HUD in connection with any MAP mortgage transaction.
12. Failure of a MAP Lender to respond in a timely manner to inquiries from the Director, OMD in accordance with this Chapter.
13. Indictment or conviction of a MAP Lender or any of its officers, directors, principals or employees for an offense that reflects on the responsibility, integrity or ability of the Lender to participate in MAP.
14. Employing or retaining an officer, partner, director or principal at the time when the person was suspended, debarred, ineligible or subject to a LDP, or otherwise prohibited from participation in HUD programs, when the MAP Lender knew or should have known of the prohibition.
15. Employing or retaining an employee who is not an officer, partner, director or principal, and who is or will be working on HUD-FHA program matters, at a time when that person was suspended, debarred, ineligible, or subject to a LDP or otherwise prohibited from participation in HUD programs, when the MAP Lender knew or should have known of the prohibition.
16. Failure to cooperate with an audit or investigation by the HUD Office of Inspector General or an inquiry by HUD into the conduct of the MAP Lender.
17. Failure to fund insured mortgage loans or any misuse of mortgage loan proceeds.

C. The issuance of a Warning Letter is not a prerequisite to the Suspension or Termination of a Lender's MAP privileges.

15.4 Administrative Record

When any final action is taken against a MAP Lender, an administrative record must be prepared which includes all materials that may have influenced the decision and not merely those relied upon in the final decision. Although not intended to be an exhaustive listing, examples of material that should be included in the record are:

- Correspondence between the Lender and HUD or the Lender and any third party contractors;
- E-mails, if relied on in the decision process;
- Fax's including the FAX cover sheet and the FAX confirmation sheet;
- Application and underwriting submissions;

- Copies of appropriate sections of notices, guide books including FAQ's posted on the Multifamily web site, handbooks, regulations and statutes;
- Notes from meetings and telephone conversations; and
- Work product and recommendations from subordinates.

The term "final action" includes issuance of a Warning Letter but does not include any referral, recommendation for action, or presentation to the Director of OMD. In matters before the Director of OMD, the administrative record ordinarily will consist of the referral and the materials accompanying the referral, any written materials submitted by the Lender and any written materials submitted by the Director of OMD in response to those materials, the transcript of the informal meeting when that transcript is a part of the record, and the final decision of the Board.

***Note*: Intra-agency memoranda and other such records should be included, but will not be *released* if privileged. The administrative record in its final form as described in this Section relates to and supports HUD's final action and is not to be released to any person outside of HUD until it has been reviewed by the Office of General Counsel. All evidentiary material supporting any recommendation to the MAP Lender Review Board must be delivered to the Lender as provided in Section 15.13.A and must be included in the administrative record.**

15.5 Warning Letters

A. The Director of OMD may issue a Warning Letter to a Map Lender.

B. The Warning Letter:

1. May require a meeting in the official's office with principal owners of, and/or Officers of the MAP Lender to discuss the problem(s) and possible corrective action(s).
2. Shall specify the violation(s) for which the Warning Letter is issued. If the Warning Letter explains or interprets a section of the MAP Guide, the text of the letter (after deleting all information that might identify the MAP Lender concerned) shall be posted on the Multifamily MAP web site as a FAQ.
3. Direct the taking of a corrective action.

C. The Warning Letter does not suspend a Lender's MAP privileges but may impose a higher level of review of the Lender's underwriting by the Hub/PC and/or Headquarters.

D. The Warning Letter must clearly state that it is a Warning Letter issued pursuant to this Chapter. The letter will be mailed to:

1. The MAP Lender's contact person as listed on the MAP website.
2. The Director, LQMD, along with a copy of the administrative record.

E. The Lender must be sent, along with each Warning Letter, a copy of the administrative record prepared with respect to that letter.

15.6 MAP Probation

Only the DAS, Office of Multifamily Housing Programs may place a Lender on probation. Probation is intended to be corrective in nature and not punitive. As a result, release from probation is conditioned upon the Lender meeting a specific requirement or requirements, such as replacement of a staff member.

A. During the probation period a MAP Lender may:

1. Not submit, and the Hub/PC may not accept, materials after the close of business of the date of the probation letter, for a new:

   a. MAP Pre-application for a Section 220 or 221(d) project involving new construction, substantial rehabilitation; or

   b. MAP Firm Commitment application for a Section 207 pursuant to Section 223(f) project involving a purchase or refinance.

   Note: If either a new Pre-application or a new Firm Commitment application for a Section 207 pursuant to Section 223(f) was accepted after the date of the probation letter, it must be returned to the MAP Lender.

2. Continue to process any:

   a. MAP Section 220 or 221(d) project involving new construction/substantial rehabilitation when a pre-application was submitted to a Hub/Program Center before the date of the probation letter.

   b. MAP Section 207 (pursuant to Section 223(f) project involving purchase or refinance when a Firm Commitment application was submitted to a Hub/Program Center before the date of the probation letter.

B. Probation continues until all corrective actions required by the OMD (for example, exclusion of a specific staff member from work on MAP loans) are taken by the MAP Lender. When all corrective actions have been taken, the MAP Lender shall notify the OMD. Once the OMD is satisfied that the corrective actions have occurred, the Probation period shall end. A false statement that corrective action has been taken constitutes a false certification as described under Section 15.3, and may constitute a violation of 18 US.C. § 1001. A Lender's failure to take prompt corrective action after Probation has become final may be the basis for Suspension or Termination.

C. Probation is in effect nationwide and the Lender's name shall be removed from the MAP-Approved Lender list on the web. When Probation is lifted, the Lender's name shall be re-posted.

D. The probation notice will be:

1. Sent by overnight delivery;

2. Addressed to the MAP Lender's contact person as listed on the Multifamily MAP website; and

3. Signed for by an employee of the MAP Lender upon receipt.

E. Refer to Section 15.12 and 15.13 for sanction and notice procedures.

15.7 MAP Suspension

Only the MAP Lender Review Board may suspend a Lender's MAP eligibility.

Suspension will not exceed 12 months except when special conditions are imposed. If both a time limit and conditions are imposed, suspension will terminate only when the time period has expired, the MAP Lender has submitted a certification of compliance with the conditions to the Board and the Board has notified the Lender it is satisfied that the corrective actions have occurred.

A. During the suspension period a MAP Lender may not:

1. Submit application materials after the close of business of the date of the suspension letter for a new:

   a. Pre-application for a Section 220 or 221(d) project involving new construction/substantial rehabilitation; or

   b. Firm commitment application for a Section 207 pursuant to Section 223(f) project involving purchase or refinance.

   If either a new Pre-application or a new Firm Commitment application for a Section 207 pursuant to Section 223(f) was accepted after the date of the suspension letter, it shall be returned to the MAP Lender.

2. Continue to process any:

   a. Section 220, or 221(d) project involving new construction/substantial rehabilitation

when a pre-application was submitted to a Hub/Program Center before the date of the suspension letter.

b. Section 207 pursuant to Section 223(f) project involving purchase or refinance when a Firm Commitment application was submitted to a Hub/Program Center before the date of the suspension letter.

B. The suspension notice will be:

- Sent by overnight delivery;
- Addressed to the MAP Lender's contact person as listed on the Multifamily MAP website; and
- Signed for by an employee of the MAP Lender upon receipt.

C. Suspension is in effect nationwide and the Lender's name shall be removed from the MAP-Approved Lender list on the web. When Suspension is lifted, the Lender's name shall be re-posted.

D. Refer to Sections 15.12 and 15.13 below for sanction and notice procedures.

15.8 MAP Termination

Only the MAP Lender Review Board may terminate a Lender's eligibility for MAP.

A. A terminated Lender may not submit, and the Hub/PC may not accept, materials after the close of business of the date of the termination letter for a new:

1. Pre-application for a Section 220 or 221(d) project involving new construction/substantial rehabilitation; or

2. Firm Commitment application for a Section 207 pursuant to Section 223(f) project involving purchase or refinance.

B. Any MAP pre-application or MAP application in process may no longer be processed by the terminated Lender. The Lender will either:

1. Immediately transfer the transaction to the TAP procedure and the Hub/PC will completely reprocess all stages of the transaction; or

2. Immediately transfer the project to a new MAP Lender. The new MAP Lender must

completely reprocess all stages of the transaction. At no time may the new MAP Lender assign the Pre-application, the firm application, the mortgage insurance commitment, or the insured construction loan back to the original MAP Lender.

C. The Department will not endorse any MAP loan processed by the terminated Lender unless a Firm Commitment was issued before the date of termination.

1. Firm Commitments involving new construction or substantial rehabilitation must be immediately transferred to a new MAP Lender. At no time may the new MAP Lender assign the Firm Commitment, or the insured construction loan, back to the original MAP Lender.
2. Firm Commitments issued for Section 223(f) projects may be transferred before final endorsement to any approved MAP Lender or kept in the Lender's portfolio.
3. For those construction loans that have been initially endorsed, the MAP Lender will lose its MAP privileges for construction loan administration. HUD will assume all the construction loan administration duties as it normally performs for TAP processing.

D. The original Lender may not service a transferred loan once it is finally endorsed.

E. An application for reinstatement of MAP authority may not be made for 12 months after the date of termination. The requirements for reinstatement shall be the same as for initial qualification and the applicant must show that the problems, which led to termination, have been resolved.

F. The termination notice is:

1. Sent by overnight delivery;
2. Addressed to the MAP Lender's contact person as listed on the Multifamily MAP website; and
3. Signed for by an employee of the MAP Lender upon receipt.

G. Termination is in effect nationwide and the Lender's name shall be removed from the MAP-Approved Lender list on the web.

H. Refer to Sections 15.12 and 15.13 below for sanction and notice procedures.

15.9 Settlement Agreements

A. The Director of OMD is authorized on behalf of the Office of Multifamily Housing to negotiate settlement agreements with MAP Lenders.

1. ***Before*** the Director of OMD has recommended a MAP Lender to the MAP Lender Review Board for possible Suspension or Termination, the DAS for Multifamily Housing or his/her

designee must approve any proposed settlement agreement.

2. ***After*** the Director of OMD has recommended a MAP Lender to the MAP Lender Review Board for possible Suspension or Termination, only the DAS for Multifamily Housing or his/her designee may approve any proposed settlement agreement.

B. Settlement agreements may provide for:

1. Cessation of any violation.
2. Correction or mitigation of the effects of any violation.
3. Removal of Lender staff from positions involving origination, underwriting and/or construction loan administration.
4. Actions to collect monies wrongfully paid by the MAP Lender to a third party.
5. Implementing or revision of a Quality Control Plan or other corrective measure acceptable to HUD.
6. Modification of the duration or provisions of any administrative sanctions HUD deems appropriate.

C. A MAP Lender's compliance with a settlement agreement is evidenced by certifying its compliance with the conditions of the agreement and by HUD determining that the Lender is in compliance with the conditions of the agreement.

D. Failure by a MAP Lender to comply with a settlement agreement may result in referral to the MAP Lender Review Board for suspension or termination.

15.10 MAP Lender Review Board

A. The Board is authorized to take action against any MAP Lender that violates MAP requirements.

B. Composition.

1. The Board shall consist of three Multifamily Housing Officials designated by the DAS for Multifamily Housing.
2. Board Members
   a. Are selected from among Hub and Program Center Directors or Multifamily Housing employees.
   b. May serve on a continuing basis or may be chosen for the particular review, as the DAS

determines.

c. Shall have no prior business affiliation or other conflicts of interest with the Lender under review.

d. Shall select one of their members to act as Chairman of the MAP Lender Review Board.

e. Are expected to have knowledge of multifamily housing origination, underwriting and construction loan administration procedures.

3. The following individuals cannot serve on the Board:

a. The Hub/Program Center Director making the recommendation;

b. Staff from the Hub/Program Center making the recommendation;

c. The Director of OMD; and

d. Staff from OMD

C. Non-voting Advisors to the Board.

1. Designee of the Office of Inspector General

2. Designee of the Office of General Counsel

D. The Director of OMD or his/her designee presents the cases to the MAP Lender Review Board

E. Functions, Duties and Powers.

1. The MAP Lender Review Board is authorized to impose appropriate sanctions on a MAP Lender after:

a. Conducting an impartial review of all information and documentation submitted to the board; and

b. Making factual determinations that there has been a violation of MAP requirements.

2. In determining what action is appropriate, the Board will consider among other factors:

a. The seriousness and extent of the violation(s);

b. Any history of prior offenses;

c. Deterrence of future violations;

d. Any inappropriate benefits received by the MAP Lender;

e. Potential inappropriate benefit to other persons; and

f. Any mitigating factors.

3. The Board may refer:

a. A MAP Lender to:

(1) The Mortgagee Review Board for possible termination as a HUD-FHA approved mortgagee or Lender, and/or imposition of civil money penalties for knowing and material violations of HUD-FHA requirements (see Section 15.17)

(2) The Office of Inspector General

b. An individual or firm involved in a "covered transaction," as defined in 24 CFR 24.110 to the DAS for imposition of an LDP which may be imposed on a nationwide basis or on a more restricted geographic basis.

15.11 Support Staff for MAP Lender Review Board

A. The Chairman of the Board supplies the clerical staff for the MAP Lender Review Board. The clerical staff:

1. Coordinates Board activities with other HUD offices and government agencies.
2. Develops the agenda and policy issues for Board meetings.
3. Notifies a MAP Lender of any sanction imposed by the Board.
4. Notifies a MAP Lender, when the Board is to consider sanctions.
5. Keeps the official minutes of the Board and the case files and all Board actions.
6. Drafts all notices, orders, letters, and directives on behalf of the Board.
7. Performs other duties assigned by the Chairman or as directed by the Board.

B. The Office of Multifamily Development staff serves as the prosecutor and:

1. Are the contacts on all matters concerning the Board.
2. Presents the sanction cases to the Board.
3. Collects, analyzes, prepares and submits to the Board the charging document and supporting documentation together with possible options or recommendations as to sanctions against a MAP Lender.
4. Refers cases for Board consideration.
5. Negotiates settlement agreements with MAP Lenders.
6. Prepares the administrative record of all matters before the Board.

C. Office of Inspector General

1. Refers MAP Lenders for Board consideration as a result of audits or investigations.
2. Performs audits or investigations of approved MAP Lenders.

D. Office of General Counsel

1. Advises the Board as to the legal sufficiency of actions it proposes to take.
2. Assists the Board in the drafting of Board decisions and orders.
3. Assists the Director of OMD in settlement negotiations.
4. Provides other legal advice as requested by the Board.

15.12 Procedures for Sanctions

A. Requests for MAP Lender Review Board Action. The Director of OMD, or his/her designee, may refer a MAP Lender to the Board for consideration of sanctions.

1. Any referral from a Hub Director must be sent to the Director of OMD.
2. The referral must contain a written report, which includes:
   a. A full factual background description of the violations;
   b. Specific citations of the Department's requirements that have been violated; and
   c. All available supporting documentation that bears upon the violations (the administrative record discussed earlier)
3. There is no notification to the Lender until the Board is constituted and receives the charging documents from the Director of OMD. (At that point, notification under Section 15.13 is automatic, and does not require substantive consideration by the Board of the nature of the charge.)

B. Appointment of the Board

When the Director of OMD intends to send a referral to the MAP Lender Review Board, s/he requests the DAS to appoint a Board, as described in Section 15.10.

C. Initial Consideration by the Board

When the Board receives a referral from the Director of OMD, the Board members may confer by email or by conference calls or in person. Any record of confidential communications between and among Board members at this stage of the proceedings is privileged from disclosure and will not be part of the administrative record of any matter.

D. Informal Conference

1. The Lender may request an informal conference as discussed in Section 15.13, which the Board will schedule.

2. After notifying the Lender and permitting the Lender an opportunity to respond, the Board will meet with the Lender or its designees and with the Director of OMD and his/her designees to review documentary evidence and presentations by both sides (see Section 15.13).

a. Transcript of the informal meeting.

(1) No transcript of this informal meeting will be made, unless the Lender elects to have a transcript made by a certified court reporter at its own expense. If the Lender elects to have a transcript made, it must provide three copies of the transcript to HUD within five business days of the informal meeting. The transcript will not become a part of the record unless it is submitted within the 5-day time frame.

(2) If a transcript is not provided within the time limit set forth above, oral statements made at the informal meeting will not be considered as part of the record, except that the Board may consider voluntary admissions, made by a representative of the Lender, of any element of the violation charged.

b. Any additional documents, evidence, or written arguments, which the Lender wishes to present to the Board, must be presented within five working days after this informal meeting.

E. Action by the Board.

1. Upon consideration of evidence submitted by the Director of OMD and the MAP Lender, the Board will confer and make a final decision regarding the matter.
2. Any final decision by the MAP Lender Review Board placing a Lender on Probation, or Suspension, or Terminating a Lender shall be in writing and shall state the reasons for the decision and the facts supporting those reasons. Higher level officials and decision makers, including the MAP Lender Review Board, are not bound by the recommendations from other HUD officials described above, except that the Board may not take any action against a Lender which is more severe than the action recommended by the Director, OMD. In any case where the action taken or the recommendation made differs from the recommendation received, that difference shall be explained in writing.

F. Effective Date of Action.

Unless the Board decrees that a later date should apply, any sanction (probation, suspension or termination) shall become effective on the date of the Notice of Action to the Lender.

F. The Lender may appeal the Board's decision to the DAS for Multifamily Housing or his/her designee, as specified in Section 15.14.

15.13 Notice of Violation

A. Before the MAP Lender Review Board reviews a matter for consideration of a sanction, the Board's Chairman will issue written notice of the proposed action to the MAP Lender's contact person as listed on the Multifamily MAP web site. The notice is sent by overnight delivery and must be signed for by an employee of the MAP Lender upon receipt. The notice:

1. Informs the Lender that the Board is considering a specific violation.
2. States the specific alleged factual violations with citation to the Department's requirements that have been violated.
3. Includes as attachments copies of all documents evidencing the violation or upon which the Board will be asked to rely in reaching a decision.
4. Provides the Lender with the opportunity, within 15 business days from the date of the issuance of the proposed action, to:
   a. Meet informally with the Board in person or by video conference using HUD facilities at Headquarters or one of the various Hub/PCs; and/or
   b. Present written evidence and any other relevant information.
5. Offers the MAP Lender the opportunity to reply in writing to the Board within 15 business days from the date of the issuance of the proposed action. Failure to reply may result in a determination

by the Board without considering the MAP Lender's comments.

6. Requires the response to be addressed to the Chairman of the Board. The response may not exceed 15 double-spaced typewritten pages and must include an executive summary, a statement of the facts, an argument and a conclusion. All written material and supporting documentation must be submitted in triplicate.

Accompanying the notice of violation is a copy of the charging document and all of the supporting documentation that has been submitted to the Board.

B. The MAP Lender Review Board has the power to issue a Notice of Action discussed in Section 15.14 to terminate a Lender, or to place a Lender on probation or suspension without advance notice to the Lender when there is an imminent need to protect the financial interests of the Government. No such action shall be taken except upon the written recommendation of the Director of OMD and approval of the DAS for the Office of Multifamily Housing Programs upon a determination by the Board that immediate action is necessary. In every such case, the Lender shall be promptly notified of the Board's decision and the reasons for it, and shall have the right to submit materials to the Board and appear before the Board to seek a prompt reconsideration of the Board's decision.

15.14 Notice of Action

A. A prompt decision is important when the Office of Multifamily Housing Programs acts to place a MAP Lender on probation. The DAS will issue the final decision within 10 business days of the receipt of the Lender's information and/or the informal conference.

B. The OMD will notify the MAP Lender of its final determination by overnight delivery of a written notice of the final decision to the MAP Lender's contact person as listed on the Multifamily MAP web site.

C. The final decision will:

1. State the nature and duration of the action.
2. State the violations and any factual findings.
3. Inform the MAP Lender of its right to an appeal conference.
4. May add or modify the reasons for the decision as stated in the initial notice.

D. A copy of the administrative record will be sent to the Lender by overnight express within one business day after the issuance of the final decision.

15.15 Appeals

A. Appeal Conference.

1. Whenever HUD imposes a sanction of probation, suspension or termination against a MAP Lender, the Lender may request in writing, an appeal conference before the appeals official Appeals Official must be an individual who has not previously involved with the proceedings

or settlement discussions up to this point.

2. No transcript of this the appeal conference–will be made, unless the Lender elects to have a transcript made by a certified court reporter at its own expense. If the Lender elects to have a transcript made, it must provide three copies of the transcript to HUD within five business days of the informal meeting.

3. Oral statements made by any participant at this meeting are not considered as evidence on any matter under consideration, except that the Appeals Official may consider voluntary admissions by a representative of the Lender of any element of the violation charged.

4. Any additional written arguments, which the Lender wishes to present to the Appeals Official, must be presented within five business days after the date of the appeal conference.

B. The appeal conference regarding the Board's action will be held within 10 business days of HUD receiving the MAP Lender's appeal request.

1. The Director of OMD provides the administrative record to the Appeals Official and points out the evidence on which the decision was made; and

2. The MAP Lender may provide oral arguments in support of its position and the evidence previously submitted. No new evidence may be submitted to the Appeals Official at this point.

C. A MAP Lender may voluntarily request and the Appeals Official may agree to have an appeal conference held more than 10 but not more than 30 business days after the date of the Lender's request for an appeal.

D. Within 10 business days after the date of the appeal conference, or the expiration of the period allowed for the submission of documents and written arguments, whichever is later, the Appeals Official makes a written determination. S/he may confirm, modify, or overturn the MAP Lender Review Board's decision.

E. If the MAP Lender does not request a conference within 10 business days of receiving the sanction letter, the right to a conference will be considered waived.

F. If the Appeals Official overturns the MAP Lender Review Board's decision, the Lender shall immediately return to an active status as a MAP Lender. The active status of the MAP Lender will be posted on the HUD web.

G. Participation in the appeal process is not a prerequisite to filing of an action for judicial review

under the Administrative Procedure Act.

15.16 Limited Denial of Participation

The criteria and procedures in this section apply to suspensions and debarments as well as to limited denials of participation. See Chapter 4 of OGC Handbook 1300.13 REV 1, Debarment, Suspension, and Ineligibility of Participants and Contractors, and HUD Regulations at 2 CFR 2424. In case of any conflict between this section and the foregoing authorities, those authorities control.

A. An LDP may be imposed upon any participant or contractor and its affiliates, except HUD-FHA approved mortgagees. Examples of participants that may be sanctioned are (but are not limited to):

1. Independent Fee Appraisers
2. Third Party Cost Analysts
3. Needs Assessors
4. Environmental Analysts and Engineers
5. General Contractors
6. Architects
7. Specific underwriters or loan analysts
2. Application Sponsors

B. Once issued, the LDP may apply to any contractor, participant or to a participating organization. For example, a specific appraiser may be issued a LDP, or an entire appraisal firm may be issued a LDP. A LDP may also apply to all affiliates of that contractor or participant at the discretion of the imposing official.

C. Conditions Warranting Referral to HQ Recommending Consideration for a National LDP.

Referral to Headquarters for recommendation for a National LDP shall be at the discretion of the Hub Director. When it is determined that the offense warrants such a measure, the Hub Director should forward all pertinent information along with a formal recommendation to the Deputy Assistant Secretary for Multifamily Housing for review. The recommendation should include:

1. All related processing associated with the case(s) that initiated the action.
2. A narrative summary detailing the description and nature of the alleged offense(s) committed.
3. A synopsis of the participant's historic performance in past cases dealing with the Department.
4. A recommend course of action to be taken.

D. Questions should be addressed to the Director of the Compliance Division of the Enforcement Center.

15.17 Referral to the Mortgagee Board or the Inspector General

A. If the Hub/PC Director determines that a MAP Lender's actions or failure to act appears to be a compliance matter justifying action by the Mortgagee Review Board, including possible removal of its authority to do business as an FHA Lender, s/he must bring this matter and the administrative record to the attention of the Director, Office of Multifamily Development in Headquarters. The Director will refer the matter to the Director of the Mortgagee Review Board Division in the Departmental Enforcement Center.

See Section 2-4, Requests for Mortgagee Review Board Action, HUD Handbook 4060.2 REV 2, Mortgagee Review Board, and HUD Regulations at 24 CFR 25.

B. If the issue involves possible fraud, material misrepresentation or other criminal violations, then the matter should be referred to the Office of Inspector General.

See Section 3-1, Responsibilities of Departmental Management and Employees, OIG Handbook 2000.3 REV-4, Office of Inspector General Activities.

15.18 Other Enforcement Actions

Notwithstanding any provisions contained elsewhere in this Guide, HUD reserves the right to pursue remedies for false claims and false statements, as authorized by the False Claims Act, 31 U.S.C. §§ 3729-3731, and the Program Fraud Civil Remedies Act, 31 U.S.C. §§ 3801-3812.

Chapter 16

Master Lease Structuring to Facilitate the use of Tax Credits

16.1 Introduction

To facilitate the use of FHA-insured loans with tax credits, the use of Master Leases on tax credit transactions is permitted, in accordance with the guidance contained in this chapter. The processing changes described in Chapter 14, "LIHTC and other Tax Credit Guidance," are available for use with Master Lease transactions, including Historic and New Markets tax credits.

16.2 Background

Master Leases are used to maximize the benefits of combining some or all of the following tax credit sources: Federal or State Historic Tax Credits, New Markets Tax Credits and Low Income Housing Tax Credits. Master Leases are advantageous to investors and developers participating in these programs by providing maximum leverage for project financing and premium pricing for equity while reducing the need for additional debt.

A Master Lease, also known as a Sandwich Lease or Credit Pass Through Lease, is used by a developer of a multifamily project to maximize the receipt of tax credit equity and distribute benefits among various investors. Typically, these leases permit a combination of investments by one or more investors under one or more tax credit programs in a single development project. The Master Lease structure differs from the more traditional ownership structure in that project assets and revenues under a Master Lease pass through a number of tiers and, in doing so, come under the control of entities other than the Borrower. HUD's goal is to allow this type of structuring without compromising appropriate regulatory oversight and controls. While complicated, these transactions must include basic obligations imposed on the Master Resident to pay the Borrower/Lessor rent that equals or exceeds the amount necessary to satisfy all financial obligations required under the insured mortgage and to operate the property in accordance with all HUD directives, regulations and contracts. To ensure compliance with such regulatory and administrative oversight and control, in addition to the Borrower/Lessor, the Master Tenant and all Master Sub-lessees (but not the individual residential and commercial tenants) will execute HUD Regulatory Agreements and submit financial reports to HUD. See Appendix 16A for a sample Master Lease ownership structure.

The Hub/PC will be responsible for approving requests to utilize Master Lease ownership structures in accordance with this chapter's requirements and may not waive any of these requirements. Any proposed waivers must be sent to Headquarters (HQ) Office of Multifamily Development, for review and approval and must include a written recommendation from the Hub Director.

16.3 Eligible Programs

Master Lease structures may be used under the following programs:

- Section 220
- Section 221(d)(4)
- Section 223(f)
- Section 231

Master Leases may be used on tax credit projects with Section 8 housing assistance payment contracts and/ or Section 236 de-couplings.

16.4 General - Programmatic Requirements

In addition to the current program requirements, the following are conditions for projects that use a Master Lease structure:

A. The Master Tenant and Master Sub-lessees must be single purpose entities; Statutory Trusts or Delaware Statutory Trusts are not eligible entities. The Master Tenant and Master Sub-lessees may not engage in any other businesses or activity, including the operation of any other rental project, or incur any liability or obligation except as permitted by HUD in connection with the project.

B. The Master Tenant and Master Sub-lessees must execute the standard HUD regulatory agreement and Rider, to address various ownership and operational responsibilities with respect to the mortgaged property.

C. The management agent must execute HUD's management certifications. The Master Tenant and Master Sub-lessees must file management certifications and management profiles. HUD must be able to terminate a management agreement, if warranted, in accordance with the terms and conditions contained in the certification and without Lender consent, to protect its interests, pursuant to the standard termination language in Section 9 (a) of the management certifications.

D. Net rentable commercial area as a percentage of gross floor area and income will be determined in accordance with the applicable program limitations.

E. The Master Lease and all Sub-leases (sometimes collectively referred to as "Leases") shall be subordinate to the insured mortgage and subject to approval by HUD prior to execution. The Leases may not be modified or amended without the prior written consent of HUD, and may be terminated by HUD in the event that the insured mortgage is assigned. Any proposed modifications or amendments to the Leases must be approved by the Hub/PC Office of Field

Counsel and Mortgage Credit. The Leases must incorporate by reference the Regulatory Agreement, HUD rules, regulations and directives, and contain an agreement to comply with their requirements. The Leases must include an obligation to pay all rent due to the Lender, in the event of a default under the loan documents. HUD will agree to allow an amendment to the loan documents authorizing that notice of default be given to the Master Tenant contemporaneously with the giving of notice to the Borrower/Lessor, and the acceptance of a cure of such default, during such notice period, from the Master Tenant on behalf of the Borrower/Lessor. Any such cure must occur prior to the assignment to HUD, and will be limited to one opportunity to cure during each 12 month time period.

F. Surplus cash determinations will be made in accordance with the Regulatory Agreements and will be made as if the entire project is owned and operated by one single purpose entity.

G. All financial operations and reporting are governed by 24 CFR, Part 5, Subpart H.

H. The rent paid by the Master Tenant must equal or exceed the monthly principal and interest payments due on the insured mortgage and all required escrows and reserves.

I. All business agreements are to be disclosed to and are subject to approval by HUD during loan underwriting (including, for example, inter or intra-company loans, investor or outsider loans other than the insured mortgage, investor controls over operations, actions and deliverables that affect regulatory or contractual compliance or performance, etc.). The Firm Commitment will incorporate any conditions imposed by HUD with respect to such agreements.

J. Any proposed payments (equity contributions, fees, income, etc.) to the Borrower, Master Tenant, Master Sub-lessees by a syndicator or investor must be disclosed to HUD and approved during loan underwriting, and thereafter be reflected on the annual financial statement filings and on any required monthly reporting. If payments are made while any party is in non-compliance with the Regulatory Agreement, enforcement action will be taken against all principals in the organization, subject to the notice and cure provisions in above subsection E.

K. Master Leases and Sub-leases must prohibit assignments or subleases (except to the end-users of the commercial spaces and apartment residents), unless previously approved by HUD in writing.

16.5 Firm Commitment Exhibits and Processing

The Lender should conduct a pre-application meeting with the Hub/PC Director before the submission of a formal application for mortgage insurance. In addition to the required exhibits, the following information should be submitted with the pre-application and/or the Firm Commitment application to facilitate a review of each transaction:

A. All layers of financing, applicable financing documents, commitments or term sheets including the loan amounts and key terms. If the Borrower/Lessor obtains bridge loan financing which is secured by future syndication proceeds, a letter from the bridge lender must be submitted which:

Certifies that the loan is secured only by a pledge of partnership interests and of tax credit benefits

and is not secured by the project and that the lender has no claim against the mortgaged property, mortgage proceeds, any reserve or deposit, or against the rents or other income from the property for repayment.

B. Full disclosure of the name and financial interest of:

1. All principals, as defined in 24 CFR 200.215(e), of the Borrower, Master Tenant and Master Sub-lessees; and
2. The general contractor.

C. Certifications are required from the following entities, disclosing all relationships between parties to the transaction:

1. All principals of the sponsor/borrower
2. Mortgagee
3. General Contractor
4. Management Agent
5. Syndicator
6. Developer
7. Master Tenant
8. Master Residential Tenant
9. Master Commercial Tenant
10. Party making an equity bridge loan, if any.

D. A Sources and Uses statement of total development costs and Form HUD-2880, Applicant/Recipient Disclosure/Update Report.

E. Certifications from Borrower/Lessor, Master Tenant, Master Sub-lessees and investor(s) that HUD has been given full disclosure of all details of the transaction structure, including the information required in Section 16.4 above with respect to business agreements and payments.

F. A narrative describing the lease agreements between the Borrower/Lessor and Master Tenant, and the Master Tenant and Master sub-lessees, detailing the collection and flow of funds from the Master Sub-lessee to the Master Tenant and from the Master Tenant to the Borrower/Lessor.

G. A market study establishing demand for any proposed commercial space in accordance with Chapter 7.

H. Previous Participation Clearance, Form HUD-2530, for the Principals of the Borrower/Lessor, Master Tenant and all Master Sub-Lessees. Tax credit investors may opt not to apply for participation clearance and instead file a Limited Liability Corporate Investor (LLCI) certification.

I. The Borrower/Lessor, Master Tenant, and Master Sub-Lessees are all subject to the standard underwriting requirements 8 of the Guide.

J. As with non-Master Lease applications, Initial Operating Deficit escrows ("IODs") will be required for all applications proposing a Master Lease ownership structure. For applications involving both residential and commercial components, separate IODs will be established for each, in accordance with program requirements.

16.6 Special Firm Commitment Conditions

The Commitment should be annotated to reflect these special Firm Commitment conditions:

A. The policies and procedures involving master lease structuring to facilitate the use of tax credits are incorporated herein and made a part of this Commitment for insurance of advances, specifically including, without limitation, the terms and conditions contained in (a) Section 16.4, entitled "Programmatic Requirements," (b) Section 16.5, entitled "Firm Commitment Exhibits and Processing," and (c) Section 16.7 entitled "Actions Prior to Initial Endorsement, thereof. Without limiting anything contained in Chapter 16, all information submitted to HUD with the Application for Multifamily Housing Project, Form HUD-92013, to evidence the satisfaction of such terms and conditions shall be true and correct as of the date submitted, and must continue to be true and correct at the time of Initial Endorsement.

B. This commitment is subject to, and has been issued upon the reliance of, the successful (a) allocation to the project of LIHTC, Historic Tax Credits or New Markets Tax Credits and (b) syndication of such credits, with an appropriate agreement for the timely investment of equity, as shown on Forms HUD-2880 and HUD-92013, to assure completion of the project and pay other associated and incidental costs. In addition to the standard provisions that must be included in the organizational documents for the borrower entity, a provision must be added that prohibits any changes to the organizational documents that affect the obligations of the tax credit investor without the written consent of the Lender and HUD.

C. Notwithstanding the issuance of this commitment, this commitment remains subject to, and HUD's obligations hereunder are conditioned upon the satisfactory resolution, as determined by HUD, of the adverse items determined by HUD during the 2530 review process.

D. As an accommodation, this commitment has been issued and based upon schematic drawings, instead of the final Drawings and Specifications. At least 30 days prior to the scheduled date for initial endorsement, HUD must receive the final Drawings and Specifications for review and approval to ensure consistency of design and cost. In the event that there is a net cumulative construction cost increase or change in the design concept, or a net cumulative construction cost decrease in the amount of more than 2%, this commitment shall be subject to and conditioned upon the further approval of the HUD, to be evidenced in writing, and may be terminated and voided by the HUD, or additional conditions may be imposed, at HUD's option.

   (See Section 5.28 for further policy guidance on the deferral of final plans and specifications at Firm Commitment when tax credits are involved.)

E. Prior to and as an additional condition of Final Endorsement, because the project is exempt from providing a cost certification, when the project reaches 100% substantial completion, as deemed by the HUD Inspector, the Lender will be notified of the substantial completion date, and the

Borrower must account for all operating income during construction and ending three months prior to the originally scheduled date of the first principal payment under the mortgage. An income and expense statement must be submitted covering the period from first occupancy (if occupancy occurred during construction) or from the date of substantial completion (as deemed by the HUD Inspector) through the period ending three months before the date of the first principal payment under the mortgage as originally scheduled. The statement must be submitted to HUD, at least 30 days before the date scheduled for Final Endorsement. If the income and expense statement evidences receipt of income net operating income during this period, the Borrower may be required to handle the funds in accordance with current cost certification guidance.

16.7 Actions Prior to Initial Endorsement

Prior to closing, the following documents will be reviewed by the Hub/PC:

A. A final detailed Sources and Uses statement of total development costs, reflecting any revisions to hard and soft costs as reflected on the firm commitment, HUD-92264. If any funding sources have changed, a revised HUD-2880 is also required.

B. The following forms will be revised to more clearly reflect the lease structure and HUD requirements:

   1. Form HUD-92434M, Lender's Certificate (formally Borrower's Certificate) - To include language that clearly states that the Master Tenant and Sub-lessees must report lease payments during the construction period as rental income.

   2. Form HUD-93305M, Agreement and Certification - To include language that clarifies that the Borrower must report all receipts and disbursements from the date of first occupancy and during the rehabilitation period for substantial rehabilitation cases.

C. Evidence that the insured mortgage is in first lien position with respect to all project collateral.

D. All documents should include conflict language giving the HUD documents supremacy over other documents and may not include indemnification provisions, except as otherwise permitted by HUD.

E. At closing, the Borrower, Master Tenant, Master Sub-lessees and investor(s) will reaffirm and certify that the information required in Section A above with respect to business agreements and payments remains true and correct. This would include any changes to disclosures of relationships discussed in Section B.

F. Each Master Lease or Master Sub-Lease must be recorded in the appropriate real estate records, s must the Regulatory Agreement executed by each Master Tenant or Master Sub-Lessee and must be included in Schedule B, Part II of the title insurance policy. In those jurisdictions where the recording of one or more of these documents would result in the imposition of a substantial tax, in lieu of recording the document(s), provisions must be added to the Borrower's Regulatory Agreement stating that any Master Tenant and Master Sub-Lessee shall be required to execute, and be bound by, a Regulatory Agreement in form and substance satisfactory to HUD.

16.8 Cost Certification and Final Endorsement

The Borrower/Lessor, the Master Tenant and all Master Sub-lessees will be required to cost certify the actual costs of the project unless the property contains tax credits and HUD determines at the time of Firm Commitment issuance that it has a loan to cost ratio of less than 80 percent. Master Lease projects containing tax credits will follow procedures described below. For all other projects, the cost certification must contain a certification signed by an authorized agent of each entity, audited by a CPA or IPA, and contain a Schedule of Tax Credit/Syndication Proceeds that includes the following:

- The amount of syndication proceeds received from the investing partner to date.
- Purposes for which syndication proceeds received as of the cut-off date were used.
- Dates, terms, and conditions under which future investor contributions are to be made.

A. Total income of the Borrower/Lessor, including lease payments, is recognized during the construction/rehabilitation period. If the replacement cost mortgage (Criterion 3) is not the controlling mortgage and there is excess NOI generated during construction, it may be applied to cover shortfalls in mortgageable soft costs, change orders, initial operating deficit and escrows. At Final Endorsement funds may be distributed to the borrower or deposited into the project's Reserve for Replacement account or applied toward the amortization of the mortgage principal.

   If Criterion 3 is the controlling mortgage amount, HUD will determine if the balance of the NOI is equal to or greater than 1% of the original mortgage amount and, if it is, will deduct this amount from the certified replacement cost. When the NOI does not meet this 1% threshold, it can be used toward shortfalls as noted above. Any remaining balance must be deposited into the project's Reserve for Replacement account at Final Endorsement and there is no distribution to the borrower. The Borrower/Lessor, Master Tenant and Master Sub-lessees are required to submit a certified operating statement which reflects the income collected and expenses incurred in accordance with the lease agreements and all documents required by HUD. Refer to Chapter 13 for further details on cost certification and the exemption from cost certification.

B. A final Sources and Uses Statement must be included in the cost certification report as supplemental information and will be reviewed to determine actual sources and uses.

16.9 Multifamily Housing Hub/PC Responsibilities

The Hub/PC is responsible for reviewing the submission to ensure that all applicable conditions have been satisfied and may approve requests to utilize Master Lease ownership structures in accordance with the requirements of this Chapter but may not waive any requirements of this Chapter. Any proposed waivers must be sent to HQ's Office of Multifamily Development for review and approval and must include a recommendation from the Hub Director.

Chapter 17

Refinancing Cooperative Housing Projects under Section 207 pursuant to Section 223(f)

17.1 Introduction

The following provides processing instructions for refinancing Cooperative Housing Projects under the Section 207 pursuant to Section 223(f). The Department is currently in the process of amending 24 CFR §200.24 to allow for Cooperative borrowers. Until the regulation is amended, it will be necessary to apply for a waiver of 24 CFR §200.24 in its entirety. The waiver request should originate from the Hub Director and be sent to the Director of Multifamily Housing Development, in HUD HQ. This applies solely for refinancing a project and does not apply to projects that include an acquisition. Please note that proposed conversions or projects undergoing conversion, to cooperatives are not eligible for refinancing under this chapter.

17.2 Background

Cooperative ownership is popular in certain parts of the country, especially for low-to-moderate-income occupants. HUD already insures traditionally processed mortgage loans to facilitate the construction and substantial rehabilitation of Cooperative Housing projects under Section 213. Facilitating the refinancing of a Cooperative under Section 223(f) will further the Department's mission by assisting eligible Cooperative projects to obtain refinancing to make necessary repairs and/or consolidate more expensive outstanding debt, thereby serving to preserve the affordable housing stock. Refinancing the existing underlying mortgage is considered to be a better alternative than expending a Cooperative's reserve fund, which would have a negative impact on its financial stability and would help to avoid the need for a special assessment, which could harm low-to-moderate income occupants, especially those on a fixed income.

17.3 Program Requirements

The Underwriting Summary must demonstrate compliance with all program requirements.

A. Loan Parameters. In accordance with Section 3.8.O, HUD will insure a mortgage for a maximum term of 35 years or 75% of the remaining economic life of the property, whichever is less. The maximum insurable mortgage amount shall be the lesser of the following parameters as they relate to the criteria in Form HUD-92264-A, "Supplement to Project Analysis": (NOTE - An equity take out from a refinancing loan is not permitted for cooperative housing projects.)

   1. Criterion 1. Mortgage or Loan Amount Requested in Application.

2. Criterion 3. Amount Based on Value or Replacement Cost. The lesser of market value, valued as a market rate rental project multiplied by a loan ratio of 65%, or the Gross Sell-off Value, as a market rate cooperative project multiplied by a loan ratio of 55% (value definitions are contained in Section II.B).

3. Criterion 4. Amount Based on Limitations per Family Unit. Use Section 207 statutory per unit limits, adjusted by the local PC High Cost Percentage for the locality. Follow the outstanding instructions for Criterion 4.

4. Criterion 5. Amount Based on Debt Service Ratio. A mortgage amount supported by 1.0 debt coverage based on the projected NOI as an existing Cooperative project, which is NOI noted on line "5.e".*

   ***NOTE**: In addition to the calculation of Criterion 5, the underwriter must perform a feasibility test comparing Criterion 5 as calculated above to a Criterion 5 calculation on a mortgage amount supported by a 1.538 debt service coverage based on projected NOI as a market rate rental project, which is NOI multiplied by 65%. This will be reported on page 4, "Remarks" of Form HUD-92264-A. If the amount based on NOI as an existing Cooperative project exceeds the amount based on NOI as a market rate rental project, the underwriter must comment on the feasibility of the project to continue as a Cooperative.

5. Criterion 7. Criterion 7 is not to be completed since acquisitions are ineligible.

6. Criterion 10. Amount Based on Existing Indebtedness, Repairs and Loan Closing Charges. Follow outstanding instructions. The cost to refinance includes funding, if applicable, the Initial Funding of the Replacement Reserve and the Initial Deposit to the General Operating Reserve (see Section 17.3.F below). No equity out is permitted under Section 223(f) when refinancing Cooperatives, accordingly, the calculation for this criterion stops at line "10.g".

7. Criterion 11. Amount Based on Deduction of Grants and Gifts and Loans. Line "11.a" shall be the cost to refinance plus FHA Mortgageable items taken from Line "10.g". Line "11.b" shall be total of grants, gifts and loan intended to offset the cost of mortgageable items. Line "11.c" shall be Line "11.a" minus Line 11.b".

B. Eligible Borrowers. Eligible Borrowers include nonprofit Cooperative Ownership Housing corporations or nonprofit Cooperative Ownership Housing trusts regulated under state law and regulatory agreements that require membership eligibility and transfer of membership in a manner approved by HUD.

C. Application Processing. Applications for Cooperatives are processed in accordance with the current Section 223(f) instructions except as modified here.

D. Required Exhibits. All exhibits normally required for a Section 223(f) application must be submitted with the following modifications and additions.

   1. Rent Roll. The Rent Roll should be modified to indicate each shareholder's name, unit location, mailing address, whether or not the unit is owner occupied, whether or not the unit is subsidized, date of occupancy, ownership percentage, amount of monthly maintenance charge, any special assessments and past due balances of 30 days or more. For any units subject to local rent control, the actual rent must be substituted for the maintenance fee amount. The Rent Roll should be submitted as an Excel spreadsheet.

2. Cooperative Membership Exhibit. Subsequent to issuance of the commitment and prior to closing, the Lender must submit a statement of the cost to the borrower and the Cooperative Membership Exhibit, Form HUD-93203. The number of members must equal the percentage (or number) of the total number of units as specified in the commitment.
3. Original Project Prospectus (if available). The prospectus is prepared at the time of the original public filing and contains a great deal of useful information for technical discipline processing by HUD as well as the underwriter and preparers of third-party reports.
4. Financial Statements for the Past Three Years. Follow the current instructions contained in Section 7.7.B and Section 8.4. The Lender should review and evaluate any qualifications contained in the reviews to ensure the financial statements reliably represent the property's operating history and the assumptions relied on in the underwriting and should pay particular attention to the history of total past due balances of maintenance fees and special assessments. The total amount of the unpaid balance (30 days or more) for maintenance charges and special assessments as shown in the rent roll must not exceed 5% of the gross annual income.
5. Environmental Exhibits.
   a. Contamination Analyses. A Phase I ESA, if necessary a Phase II ESA, and, if further necessary, a remediation plan are required. See Chapter 9.
   b. Environmental Report. As described in Chapter 9, an Environmental Report is required.
6. Additional Third-Party Reports. HUD may require additional specialized reports to ascertain the safety and soundness of the property and its amenities as to their suitability as collateral for long-term financing.
7. Organizational Documents and Minutes. The Hub/PC will provide the documents set forth in Handbook 4550.3, Existing Construction – Cooperative Housing. The following additional exhibits are required:
   a. Certificate of Incorporation FHA Form No. 3234-B.
   b. Resolution of Board of Directors to Mortgage Cooperative.
   c. Shareholders authorization to Mortgage Cooperative.
   d. Resolution of Board of Directors adopting FHA Form No. 3245, "Model Form of By-laws."
   e. Shareholders authorizing adoption of FHA Form No. 3245, "Model Form of By-laws."
   f. Minutes of the last six Board of Directors meetings.
   g. Resolution of Board of Directors adopting FHA Form No. 3237, "Model Form of Occupancy Agreement."
   h. Resolution of Board of Directors adopting FHA Form No. 3237-A, "Model Form of Sublease."

E. Project Eligibility. The property must contain at least 5 residential units with complete kitchens and baths, and have been completed or substantially rehabilitated for at least 3 years prior to the date of application. Properties that were substantially rehabilitated with HUD-insured mortgages that have been completed with an expired latent defects guarantee are exempt from the Three Year-Rule. If the Cooperative was a conversion, the conversion must have been completed at least three years prior to the application date. Proposed conversions or projects undergoing conversions are not eligible. Projects with a recent or unresolved vacancy history, or a history of

shareholders not paying dues, maintenance fees and other co-op obligations, will not be considered for mortgage insurance. The project must be fully subscribed, with no units owned by the original developer, prior to endorsement and must meet these additional criteria:

1. Project Design. The project must be designed for primary residence only. Timeshares, resorts, Cooperative hotels or rental pools are not permitted. Section 513 of the National Housing Act prohibits the use of the insurance programs for transient or hotel purposes. The borrower and individual shareholders cannot execute Occupancy Agreements for less than 30 days nor provide occupants with hotel services such as maid service, furnishing and laundering of linens, room service and bellboys. Units may not be sub-leased without the consent of the Cooperative Corporation.
2. General Market Conditions. The Property must be located in an area evidencing strong market understanding and acceptance of Cooperative housing. Financing for the purchase of individual shares must be readily available from mortgage bankers/brokers, banks or saving and loan institutions. The Underwriting Summary must cite recent sales within the building and indicate the type of financing utilized.
3. Repair Threshold. A project cannot be processed under Section 223(f) if it meets the current requirements for substantial rehabilitation in Section 5.12. Projects that are not eligible for mortgage insurance under Section 207 pursuant to Section 223(f) should consider the Section 213 or Section 221(d)(3) programs.
4. Fair Housing Act / Equal Opportunity Requirements. All other applicable program requirements for the Section 207 pursuant to Section 223(f) program must be met, including compliance with applicable Civil Rights Laws, including the nondiscrimination and affirmatively furthering fair housing provisions of the Fair Housing Act, and applicable accessibility requirements for persons with disabilities.
    a. Affirmative Fair Housing Marketing. The Affirmative Fair Housing Marketing Requirements (24 CFR Part 200, Subpart M) apply to all insured projects of five or more units but projects insured under Section 207 pursuant to Section 223(f) are exempt from the submission of a written plan. However, a Section 223(f) applicant is required to maintain records of its affirmative marketing efforts. Except in the case of a project specifically designed exclusively for the elderly (see below), the borrower must certify that it will not discriminate against families with children.
    b. Accessibility for Persons with Disabilities. This is required for properties built after March 13, 1991, containing Fair Housing Act noncompliance. If a project built after March 13, 1991, is submitted for Section 223(f) refinancing and the PCNA inspection reveals that it contains noncompliance with the Fair Housing Act design and construction requirements, the Department must require that the owner correct the noncompliance as a condition of insurance. The extent of the noncompliance and the cost of correction will determine whether the project is feasible as a Section 223(f) or whether to resubmit it as a substantial rehabilitation. In no case may the Department insure projects with outstanding Fair Housing Act noncompliance.
5. Elderly Developments - (aka Golden Age Cooperatives). In refinancing of the underlying mortgage for an existing Cooperative project designed for the elderly, the Department defines the term “elderly person” in the National Housing Act (NHA) as a household composed of one

or more persons at least one of whom is 62 years of age or more at the time of initial occupancy. Waiver of this definition is not permitted under any circumstances. It is noted that this definition differs from the definition in use for Section 213 of the NHA. The Cooperative shall not provide mandatory meals and services such as those associated with retirement service centers. No non-shelter services can be a mandatory condition of occupancy and must be reviewed by the Lender and approved by the Hub/PC for reasonableness. Non-shelter spaces already constructed for projects with current HUD-insured mortgages may include formal dining areas with meal services to be provided on an optional basis. All Cooperatives can provide modest kitchen equipment in a non-shelter space for the use of occupants or for catering services. The kitchen should be sufficient in size to support sanitary requirements. Additional requirements related to the provision of meals are as follows:

a. Any meal service must be provided on an optional basis.

b. The cost of meals may not be included in the residents' rental charges.

c. The costs associated with the operation of the meals service are the responsibility of the entity that operates the optional meal service.

d. The borrower may receive payment from the operator of the meals service. In such cases, this revenue may not be included in the underwriting of the project, as this service is optional for each resident, thereby potentially producing a revenue stream that is both unpredictable and unreliable.

e. A determination should be made by the Lender that the expenses associated with a third-party meal provider will not increase the project risk.

f. Any meal service must be operated by a meal provider licensed under State or local law and in compliance with current health and safety requirements for food service providers.

g. Local HUD Counsel must determine that the granting or revocation of any licensing required to operate a proposed meal service will not jeopardize the ability of the project to operate as Cooperative Housing in accordance with the requirements of the Regulatory Agreement.

h. Costs associated with developing a facility insured under Section 223(f) to include a meal service may be considered in the mortgage, subject to outstanding requirements limiting non-shelter space and commercial areas.

6. Owner Occupancy. At least 75% of the total number of residential units must be owned and occupied by Cooperative members at the time of endorsement, and no more than 25% of the units may be owned by investors.

7. Vacancy Rate. The project should not have a vacancy rate greater than 5% since a higher vacancy rate may indicate a weak or problematic project or market. If an application is presented with a higher vacancy rate, the underwriter must provide convincing market evidence to support the transaction in the Underwriting Summary.

8. Turnover Rate. The sales history of the complex should display a healthy turnover rate to demonstrate that the project is viable and that there is demand for the units. If the turnover rate is less than 5% of the total number of owner-occupied units per year, the underwriter must determine the reasons for the low turnover rate and why it does not pose an unacceptable risk, which must be documented in the Underwriting Summary. However, it should be noted that a

project and/or market area may have a historically low turnover rate due to its popularity as a source of affordable housing.

9. Adequacy of the Proposed Carrying Charges. The carrying charge must be sufficient to adequately maintain the project at a level that would make it suitable as security for a long-term mortgage. The Underwriting Summary must contain an analysis of the Appraiser's findings regarding the adequacy of the proposed carrying charge that will be in place after refinancing has occurred and a discussion of the Cooperative project's policy and history regarding increasing the carrying charge. The Cooperative's Bylaws or other appropriate organizational documents must contain a provision that requires an annual increase in the carrying charge based on inflation, in order to address increases in operating expenses.

10. Carrying Charge Increase. In general, the debt service resulting from the proposed mortgage should not require a carrying charge increase of more than 5%, which may be exceeded, so long as all of the following requirements are met:

    a. The carrying charge is below market for properly maintained similar projects, and is not sufficient to adequately maintain the project.

    b. The Board of Directors must approve the carrying charge increase in accordance with its By-laws the FHA Model Form of By-laws, FHA Form No. 3245.

    c. An analysis of the demographic data in the appraisal report must indicate the new maintenance fee would be affordable for the typical resident.

    d. Market analysis of the proposed maintenance carrying charge indicates that it is within market limits for similar projects in the subject's market area.

11. Commercial Space Limitations. The current Section 223(f) parameters must be followed.

12. Ownership of Commercial Space/Parking. Commercial and parking space at a Cooperative Housing project may or may not be owned by the Cooperative. Only those spaces that are owned by the Cooperative may be included as part of the collateral.

13. Ground Leases. Ground Leases must conform to the FHA Lease Addendum Form HUD-92070M. The term of the lease addendum may be varied to conform with applicable State and local law, except that the local HUD Closing Attorney must approve:

    a. The legal need for any proposed lease term changes, and

    b. That any term changes are consistent with the following requirements:

        (1) Term is 99 years and is renewable, or

        (2) Term is at least 50 years from the date the mortgage is executed (where a lease is on trust/other land on a reservation the HUD Closing Attorney must ensure that the lease provisions are coordinated with Bureau of Indian Affairs' requirements).

F. General Operating Reserve (GOR). Cooperatives are required by the Regulatory Agreement, FHA Form No. 3225 to establish and maintain a GOR which is a percentage of the monthly carrying charges. The carrying charge is the sum of all project expenses, replacement reserve, taxes and debt service.

1. GOR formula.

    a. The GOR is maintained by a monthly payment of 3% of the monthly carrying charges.

b. When the GOR account reaches 15% of the annual carrying charges, the monthly rate may be reduced to 2%.

c. When the GOR account reaches 25% of annual carrying charges, monthly accruals may be discontinued until the account is reduced below 25%.

d. Anytime the GOR falls below the 25% level, monthly payments to the account shall be resumed at a 2% to 3% rate, as noted above, until the 25% level is restored.

2. In addition to any Initial Deposit to replacement reserve, the Cooperative borrower may be required to make an Initial Deposit to the GOR not to exceed 15% of the annual carrying fee. The Initial Funding of the GOR using this provision may be included in the cost of refinancing up to an amount equal to 15% of the annual carrying fee.

G. Model Forms and Closing Documents. Use Handbook 4550.3, Existing Construction – Cooperative Housing, Appendix III (modified for Section 223(f)). Cooperative Organizational forms and documents must be reviewed and approved for legal and programmatic compliance before the issuance of a Firm Commitment. Use FHA Required Closing Instruments, FHA Form No. 3257-B, also set forth in Handbook 4550.3, Appendix 3-10. (See Section 17.3.D.7 above). The Hub/PC will provide the documents set forth in Handbook 4550.3.

17.4 Program Requirements – Technical Processing

A. Architectural and Cost Processing for Cooperatives. Follow the current instructions for Section 223(f). A summary of these procedures is outlined below.

1. Architectural Analysis. Lender will submit and HUD will review deliverables as specified under the present guidance for Section 223(f) to the Hub/PC.

2. Cost Processing. The HUD Cost Analyst will review Lender exhibits as required in Chapter 6 and will recommend either acceptance or rejection of the Cost portion of the Firm submission.

3. PCNA. The primary purpose of the PCNA for a Cooperative project is to assess the Capital Needs of the project with the exception of any elements owned by the individual shareholders. So, it is very important to ascertain exactly what items are the sole responsibilities of the Cooperative. In some cases, appliances, kitchen cabinets, etc. may actually be owned by the Cooperative. The interior of individual units are still inspected in the same manner as with apartments. Any hazards or defects that would affect safety and marketability of the Cooperative should be noted even if it is an individual shareholder's responsibility. These items must be corrected at the shareholder's expense prior to endorsement. Mortgage proceeds must only be used for repairs of property owned by the Cooperative.

B. Valuation Processing - Appraisal Scope-of-Work for Cooperatives. There can be great variation in how a Cooperative is structured. According to the USPAP, the determination of Scope-of-Work is an ongoing process in an assignment. Information or conditions discovered during the course of an assignment may cause the appraiser to reconsider the scope-of-work. Therefore, the guidance set forth below may be modified on a case-by-case basis to assure compliance with USPAP and that the results of the appraisal assignment will be reliable for making underwriting decisions.

There are four major elements for the appraisal assignment: General Requirements, Valuation as a Market Rate Rental Project, Market Analysis for Continued Use as a Cooperative, and Hypothetical Gross Sell-Out Value as a Cooperative.

1. General Requirements.

   a. Selection of the Appraiser. The Lender must select a qualified Appraiser in accordance with Chapter 7. It should be noted that the appraisal of a Cooperative is very specialized. Lenders should base their selection of an Appraiser on their experience for this type of assignment and upon their familiarity with the subject's market area.

   b. Value Definition. Appraisers must use the following definition published by Federal Regulatory agencies:

      "Market value means the most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby;

      (1) buyer and seller are typically motivated;

      (2) both parties are well informed or well advised and acting in what they consider their own best interests;

      (3) a reasonable time is allowed for exposure in the open market;

      (4) payment is made in cash or by financial arrangements comparable thereto; and

      (5) the price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale."

      The value shall be estimated assuming that all repairs have been completed as of the date of the appraisal.

   c. Inspection of the Subject and Comparables. The primary appraiser designated by the Lender and accepted by HUD must physically inspect the subject (both exterior and interior) and all of the comparables used as part of the analysis and must sign the Certification within the appraisal report and the supporting HUD forms.

      (1) The primary appraiser must inspect at least one of each bedroom/unit type. The total number of units inspected must equal or exceed 5% of the total number of units for projects of up to 200 units, or 4% of the total number of units/beds for projects greater than 200 units. If the characteristics and/or condition of the subject indicate that a higher level of inspection is necessary, it is the appraiser's responsibility to expand the scope of the work as is necessitated by the observations made by the primary appraiser during the inspection of the subject. This is especially important where the improvements are high-rise structures whereby individual units within demonstrate varying degrees of light and view qualities. If there are hazardous conditions or other factors that preclude a thorough inspection of the interior, the appraiser must clearly indicate these circumstances in the appraisal report.

      (2) Large Projects. For projects exceeding 500 units, the appraiser must consult with the processing office to agree on a reasonable number of units to be inspected. In addition,

the appraiser may employ assistants to inspect individual units. The purpose of allowing assistants is to encourage a thorough inspection. The names and qualifications of these assistants must be disclosed in the appraisal report but they are not required to sign the report.

(3) The primary appraiser must inspect all of the comparables used in deriving an estimate of value, including land comparables (if applicable), improved comparables sales, expense comparables and rental comparables. The appraiser must verify the condition of the comparables at the time of transfer/rental with management or other personnel familiar with the property. Contact information must be documented in the appraisal report.

d. Required Appraisal Report Exhibits. In accordance with the requirements of Chapter 7 and the programmatic requirements of Section 223(f).

e. Review of the PCNA and Phase I ESA. The appraiser must review the PCNA and ESA prior to completing the assignment, comment on any remarkable findings and their impact (if any) on value.

f. Required Approaches. In accordance with the requirements of Chapter 7 and the programmatic requirements of Section 223(f).

g. Estimation of Remaining Economic Life (REL). In accordance with the requirements of Chapter 7 and the programmatic requirements of Section 223(f).

h. HUD Forms. All of the usual forms for Section 223(f) should be employed, (92264, 92264-A, 92273 and 92274) following the outstanding instructions for Section 223(f). The Form HUD-92264 shall be completed based on usage as rental apartments. The Gross Sell-Out Value should be summarized in Section "O"; (Remarks).

i. Additional Appraisal Work Required by the Lender or other Intended Users. The appraiser is bound by USPAP to complete the appraisal assignment in compliance with the requirements of the person or entity who ordered the report and to satisfy the needs of identified intended users.

j. Reconciliation and Conclusion. The appraiser must briefly reconcile the information presented; clearly indicating what data is the most relevant and supports the report's conclusions. The conclusions must indicate whether or not the subject can expect to enjoy long-term use as a Cooperative; and whether or not the proposed maintenance fee is within market limits and is affordable for the typical shareholder.

k. Report Content and Format. In accordance with the requirements of Chapter 7.

2. Valuation as a Market Rate Rental Project. Follow all current procedures in Chapter 7 for Section 223(f) Appraisal and Appraisal Review, including these additional instructions:

a. Use of the Subject. The appraiser shall assume a hypothetical use of the subject as a market rate rental project, except that income from any units subject to rent control will assume the current controlled rental amount.

b. Estimate of Effective Gross Income. The estimate of Effective Gross Income shall be made using market rental housing comparables that are equivalent to the subject in location, size and style. Actual rents should be used for any rented units in the Cooperative that are subject to rent control. Market rents must be used for any subsidized units.

Vacancy and collection losses should also be market derived, but in no event will a residential occupancy rate greater than 93% and a commercial occupancy rate greater than 80% be used.

c. Expense Analysis. The Expense analysis should accurately reflect usage as a market rate rental project. Appropriate weight should be given to the most recent three year history for items such as repairs, maintenance and common utilities. Other items such as taxes and management expense should be based on rental apartment market data.

3. Market Analysis for Continued Use as a Cooperative. The appraisal report must also contain a Level C Market Analysis of the local market with an emphasis on Cooperatives. The purpose of the analysis is to determine the ability of the subject to continue usage as a Cooperative Housing project. The detailed requirements for performing a Level C analysis can be found in "Market Analysis for Real Estate", published by the Appraisal Institute. The study must also address these additional requirements.

   a. Assumptions. The study should assume that management has budgeting and operations under control; which can be demonstrated by an illustration of past years maintenance charge history.

   b. Financial Statement Review. Special Assessments should be explained, and a review of the last three years financial statements is required. (See Section 17.3.D.4 above for specifications for financial statements). The footnotes to the Cooperative's yearly financial statement are a typical source of details regarding past, current and upcoming issues. There should be a discussion of any material or atypical items as to their impact on value. In addition, the appraiser will complete a Form HUD-92274 using comparable Cooperative projects and also analyze the past three years records and any unaudited records from the most current period, if deemed reliable, to ascertain if the proposed maintenance charge is adequate to continue operations.

   c. Cost of Occupancy/Cost of Ownership Analysis. The typical monthly maintenance charge by unit type should be compared to the competing project's monthly maintenance charges by unit type and will serve as a variable for Cost-of-Occupancy/Cost-of-Ownership calculations to ascertain and support market-oriented unit pricing. The appraiser will complete a Form HUD-92273 for each major Cooperative unit type using other units from other Cooperative projects as comparables to compare monthly maintenance fees and to determine if the proposed monthly fee is realistic and affordable for the subject's market area.

4. Hypothetical Gross Sell-Out Value as a Cooperative. The appraiser will develop a value estimate based on a Gross Sell-Out of all units, using comparable sales analysis and any other industry acceptable methods, before the application of all costs and entrepreneurial profit associated with a conversion from a rental property to a cooperatively owned property and further assuming a vacant and moderately renovated unit. Additionally, this value is over and above a pro rata share of an underlying mortgage encumbering the premises. Based on the proposed mortgage refinancing, it is considered that such debt conforms to the influencing market parameters. A sample breakdown of the Gross Sell-Out Value is as follows:

Gross Sell-Out Value:	
Gross Sell-Out for Residential Units (453 Rooms x $48,000/Rm)	$21,744,000
Unpaid Balance of Underlying Mortgage	$2,858,300
Total Gross Sell-Out Value and Underlying Mortgage	$24,602,300
Rounded	$24,600,000

5. Appraisal Review. HUD Multifamily Staff Appraisers will review the appraisal in accordance with USPAP Standard 3. The appraisal review must include a comparison of the subject's proposed monthly maintenance fees based on the new financing to what the various units would rent for if the subject were operated as a rental project. A Cooperative Housing project's feasibility for continued use as a Cooperative is questionable if monthly maintenance fees significantly exceed what units could actually rent for. A downward trend in rents versus no change or an upward trend in maintenance fees is an indication of an unhealthy Cooperative Housing project/market.

C. Environmental Processing. The HUD Review Appraiser will follow all applicable instructions in Chapter 9.

D. Mortgage Credit Processing. Follow the current procedures in Chapter 8 for Section 223(f) modified as follows:

1. Determination of the Acceptability of the Cooperative Corporation.

   a. BOD Performance History. In processing an application, the Lender will take into account the BOD's ability and willingness to manage the Cooperative within the requirements of Section 223(f). The Lender will also consider all applicable requirements contained in Chapter 10, Management Analysis.

   b. Ability to Close. It must be determined that the Cooperative organization has the ability to close the transaction in a satisfactory manner and that the sum of the monthly charges to members will be adequate to meet debt service and other ownership expense. It must also be determined that the present members of the Cooperative, as a group, have the ability to provide whatever additional funds may be required to close the transaction.

   c. Credit-Worthiness. It must also be determined that participants have not been debarred or subject to a Limited Denial of Participation, and are otherwise capable of meeting their ownership and management obligations. For the Single Asset Borrower Entity, its Officers and BOD Members, and the Management Agent, the review should include the following documents:

      - HUD-92013 SUPPLEMENT
      - HUD-2530 / APPS Clearance
      - Verification of Deposits

   d. Other Business Concerns. List of other business concerns, are required for the Officers of the BOD.

e. Adequacy of Monthly/Annual Charges. The underwriter must ensure that the sum of monthly charges, as listed on Cooperative Membership Exhibit, converted to an annual basis, is sufficient to meet the HUD estimate of debt service, Cooperative operating expenses, taxes, special assessments and ground rents, if any, plus a general operating reserve of 3% of these items. In making these determinations of allowances for accessory income (if any), the allowance shall not exceed the Cooperative's estimate or the appraiser's estimate of accessory income, whichever is the lesser. However, rental payables under duly executed acceptable leases for commercial space on the premises shall be used in lieu of estimates. These payables should be totaled to be sure all members have assurance that the total membership has their required minimum equity requirements. The HUD estimate of annual charges will include the following:

- Debt service payments.
- Cooperative Operating Expenses, Reserve for Replacements, Taxes, Special Assessments and Ground Rent, if any.
- (Memorandum attached to Form HUD-92264). General Operating Reserve of 3% of Sum of Above.

f. Review of the Cooperative's Procedure for Approving New Members. The procedures employed by the Cooperative in approving new members (cooperators) should be reviewed to ascertain if there is compliance with any income requirements and credit scores as contained in the Cooperative's bylaws or other related agreements. Individual files for anyone becoming a member in the three month period immediately prior to the date the application for Firm Commitment was submitted must also be reviewed by the HUD processing office.

g. Maintenance Charges. The Hub/PC must review the procedures employed by the Cooperative in reviewing its budget, determining the adequacy of the carrying charge and to its history of carrying charge increases. The Cooperative's Bylaws or other appropriate organizational documents must contain a provision that requires an annual increase in the carrying charge based on inflation, in order to address increases in operating expenses. The total amount of the unpaid balance (30 days or more) for carrying charges and special assessments as shown in the rent roll must not exceed 5% of the gross annual income.

2. Determination of Total Debt Service, Cooperative Operating Expense and GOR. Total Debt Service will be calculated by multiplying the amount of the mortgage by the sum of initial curtail rate, interest rate and MIP. Cooperative Operating Expense includes those operating expenses, reserve for replacements, taxes, special assessments and ground rents, if any, which are the responsibility of the Cooperative membership as a whole rather than of the individual members and will include the cost of occupancy of the units assigned to employee use. The GOR is 3% of the sum of the annual charges described above, and is accumulated as a special reserve in order to meet possible contingencies.

3. Outstanding Debt. Past due accounts payable and outstanding project liabilities must be cleared and released, or otherwise fully satisfied, prior to or at loan closing. Examples of such items include deferred management fees, overdue utility bills or real estate taxes, or trade payables. These items are not to be included in the eligible debt basis.

4. Completion of the Form HUD-92264-A and Determining the Maximum Insurable Mortgage. Pages 1-2 of the form HUD-92264-A shall be completed according to existing instructions, modified as noted in Section 17.3.A.

D. Asset Management Processing. The application must include the applicants' management plan, including training requirements, and a description of maintenance procedures and management of the Reserve for Replacement funding and work items.

17.5 Program Requirements – Issuance of Firm Commitment and Loan Closing

Follow Section 223(f) closing procedures in the Multifamily Closing Guide and contact the Hub/PC for the FHA Required Closing Instruments, FHA Form No. 3257-B, set forth in Handbook 4550.3, Appendix 3-10.

NOTE: The MAP Forms contained in this Appendix that are used by Lenders and by HUD processing staff will be updated, revised and reissued in a Housing Notice after the Department has completed work that is currently underway to streamline application processing and program requirements. The Forms are otherwise unchanged. A new section to the Appendix has been added which contains the requirements for the Washington Docket.

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4A.I.8	Active Partner Performance System Participate Certification Form 2530 (electronic or paper certification) for all phases/stages of processing.
4A.II.A.39	Added Financial Requirements for Closing.
4A & 4B	Concept Meeting exhibits added.
4B & 4D	Removed appendices for Section 232 program.
	Architectural Analysis
5A	Section 231 added to Sections 220 and 221(d)
5A.J.2.a (2)	Corrects ALTA/ACSM MSDR from 1997 to 2005.
5A.J.2.b (2)	Corrects ALTA/ACSM MSDR from 1997 to 2005.
5A.O	Energy code changed from CABO 1992 to IECC 2006. Encourages the use of Energy Star products.
5B	Section 231 added to Sections 220 and 221(d)
5BF	References Appendix 5D, paragraph B for fire protection.
5C.C.4	Clarification on Smoke Detectors. Specific types of battery-operated smoke detectors are permitted.
5C.C.4.b	Smoke detectors are Critical Repairs for Section 223(f) projects.
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	deferred until after Initial/Final Closing.
5C.F	New - Survey requirements for Section 223(f).
5D.B.1	Fire safety requirements for substantial rehabilitation and Section 223(f) projects.
5D.B.1.b	Smoke detectors are Critical Repairs for Section 223(f) projects.
5D.B.4	Fire safety requirements for substantial rehabilitation must comply with NFPA new construction requirements.
5E.I	Removed references to FEMA-273 with FEMA-310 & FEMA-356.
5E.A.2	Signature requirements expanded to include administering Architect and Lender.
5E.A.2	Signature requirements expanded to include administering Architect and Lender.
5E.A.2	Signature requirements expanded to include administering Architect and Lender.

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5E.A.2	Signature requirements expanded to include administering Architect and Lender.
5E.B	Clarification of drawing numbering requirements.
5E.R.4	Clarification of specification numbering requirements.
5E.R.4.a	Adding Lender's name and title to the identification Cover Sheet.
5F	Changed heading to Construction Specification Institute Format
5G.1.B.2	Deletes "Structural Adequacy" as a review requirement.
5H.II.C.4	For multiple building projects, the Project Inspection Report must be itemized for each building.
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5H.II.C.5.c	New repair category: Fair Housing Act compliance-related modifications and retrofits.
5H.II.C.5.d	Owner-proposed improvements to enhance property value are

	categorized as Non-Critical Repairs.
5H.II.C.7.b	New repair category: Fair Housing Act compliance-related modifications and retrofits.
5H.II.F.1	Addition of third repair category covering properties with Fair Housing Act noncompliance.
5H.II.F.1.a	Properties with Fair Housing Act noncompliance must be modified/ retrofitted.
5H.II.F.1.b	Requires Needs Assessor to hire qualified LBP and asbestos inspectors and abide by regulatory requirements. Contractor must provide an O&M plan for any LBP and/or asbestos remaining in place.
5H.II.F.1.d	New - Seismic repairs under the 223(f) program should be treated as non-critical unless there are circumstances that warrant otherwise.
5H.III.C.1.a	New - Lender must certify that there is an Operations and Maintenance (O&M) Plan for Lead Based Paint and/or asbestos.
5H.IV.A.2	New - Items involving any repairs, rehabilitation or construction shall not be included in the Replacement Reserve Account.
5I.1	New Appendix - Certificate of Professional Liability Insurance
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Appendix 6 TOC	6D - Example of calculating CNA for new construction and sub rehab.
6A.2.B.2	Evidence of front end loading eliminated from HUD analyst's review.
6C	Revision and new instructions for determining Rehab Cost not Attributable, including revision of Rehab CNA worksheet
6D.C.4	Addition of SNA calculations for New Construction projects and a new CNA example for Sub Rehab projects.
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7B	New – Value Definitions for HUD Multifamily Appraisals, replaces the former appendix on Market Studies for Residential Care Facilities
7C.1.D.2 [C.2, C.3]	MAP Lender's appraiser use of HUD insured project as expense comparable.
7C.1.D.3 [C.2, C.3]	Confirmation of expense data in FASS.
7C.1.E [C.2, C.3]	Occupancy % must be entered.
7C.1.I.2 [C.2, C.3]	Expense per unit and expense ratio must be entered.
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7C.2.B.8	PGI, Occupancy %, Expenses and NOI are now required entries.
7C.1.H.5 [C.2, C.3]	Length and Amount of Operating Deficit now required.
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8B	The annual basic statutory mortgage limits are now found on hud.gov.

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12A.A.1.a	Disburse cash escrow funds for onsite construction before insured mortgage proceeds.
12A.A.5	New - Procedure for the disbursement of LIHTC, Historic Tax Credits and New Market, Tax Credits.
12A.C.5 NOTE	The FHA fee for bond-financed projects is capped at 5.5%. Any amount in excess of the 5.5% is not mortgageable.
12A.C.6.e NOTE	Fees for the Lender and legal services are included in the land value.
12.A.D.1.a.(4)	Added 2% working capital construction contingency escrow.

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13A & 13B	New appendices for Specimen Letters 13A, Reopening of Mortgage and 13B, Deferment of Principal Payments.

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Lender Guidelines for a Quality Control Plan

Background 2A

As a condition of receiving or continuing to receive Multifamily Accelerated Processing (MAP) privileges, Lenders must have and maintain a Quality Control Plan (QC Plan) for underwriting and construction loan administration, if applicable, of insured mortgages processed under the MAP procedures. Each MAP Lender must develop and maintain an acceptable QC Plan and conduct quality control using the guidelines below.

On January 30, 2004, the Department issued Mortgagee Letter 2004-06, a revision to Chapter 6 (Quality Control Plan) of HUD Handbook 4060.1, REV-1 CHG-1, Mortgagee Approval Handbook. Part A (Overall Requirements) applies to multifamily Lenders as well as single-family mortgagees, but is written primarily for single-family operations. Parts B, C, and D are for single-family mortgagees only.

This Quality Control Plan of the MAP Guide incorporates, for MAP Lenders, parts of Part A of Mortgagee Letter 2004-06 which are relevant to multifamily. Part E (Quality Control for Multifamily Servicing) of Mortgagee Letter 2004-06 is applicable to MAP Lenders as well as other multifamily mortgagees.

Lender Application Requirement, Exhibit M 2B

A Quality Control (QC) Plan is a required exhibit in the Lender's application package for MAP approval. The Lender will include the QC as Exhibit M of the application package, as in accordance with the instructions set forth in this Appendix.

Policy Objectives 2C

The primary objectives of the QC Plan are to assure:

A. The MAP Lender operates at a high quality performance level in the origination, underwriting, construction loan administration and closing of MAP processed multifamily insured projects.

B. The MAP Lender operates in full compliance with the National Housing Act (NHA), HUD-FHA and MAP requirements and its own policies and procedures.

C. The MAP Lender adheres to the MAP Guide policies and procedures, the MAP Forms Book and clarifications and revisions in Frequently Asked Questions (FAQ), applicable regulations, Mortgagee Letters, HUD Notices and HUD Handbooks, and internal controls.

    1. These policies and procedures are distributed to and consistently followed by its personnel.
    2. These policies and procedures are supported internally by appropriate training and staff development activities.

D. The MAP Lender’s third party contractor(s) involved in a MAP project are familiar with, understand and adhere to the MAP Lender's policies and procedures regarding quality control.

E. The MAP Lender's operating procedures are revised in a timely manner to:
    1. Accurately reflect any and all changes in HUD-FHA and MAP regulations, policies, directives or instructions;
    2. Keep all affected, accountable personnel informed and trained so as to guarantee an immediate compliance thereto; and
    3. Assure that all employees and third party contractors are held accountable for performance failures, errors and omissions.

F. The MAP Lender utilizes a program of internal and external audits that provides for an independent review by MAP Lender’s staff and/or contractor(s) who are knowledgeable and have no direct MAP loan origination, underwriting or construction loan administration responsibilities.

General Requirements of a Quality Control Plan

2D

The QC Plan must clearly describe the requirements for the MAP loan origination, underwriting and construction loan administration. The QC Plan must also state the actions the MAP Lender will take to assure acceptable management and comprehensive risk reduction in the lending process.

1. Each office of the MAP Lender, including its branches must maintain or have direct access to copies of the NHA and all HUD issuances, including Part 24 CFR regulations, HUD handbooks, Mortgagee Letters, HUD Notices, MAP Guide, MAP Forms Book, MAP Frequently Asked Questions (FAQ's), etc. which are relevant to the MAP Lender's HUD-FHA MAP origination, underwriting and/or construction loan servicing activities.

   The documents in A. above must be:

   1. Accessible to all employees and third party contractor(s);
   2. Periodically reviewed with appropriate staff and third party contractor(s); and
   3. If maintained in paper format, kept current.

2. The quality control plan must confirm the following about the Lender's place of business:

   Operations are conducted in a professional, business-like environment. If located in a commercial space, the office is properly and clearly identified, has adequate office space and equipment, and is separated from any other entity by walls or partitions (entrances and reception areas may be shared). If located in a non-commercial space, the office has adequate space and equipment. If it's open to the public, it should be accessible to people with disabilities, including those with mobility impairments.

C. The MAP Lender has procedures in place to:

   1. Distribute any electronic information received from HUD to the appropriate employees and third party contractor(s).

   2. Notify LQMD of any change in the MAP Lender's:

o Point-of-contact for the MAP procedures

o Name

o Address

o Email address

o Telephone and/or FAX numbers

o Underwriter(s)

o Construction loan administrator(s), if applicable; and

o Authorized signatory(s).

3. Provide annual certifications signed by an authorized signatory of the MAP Lender.

   a. The annual certification must be submitted to LQMD in Washington, DC no later than June 30th of each year.

   b. The certification must:

      1) List the names of the lender's approved MAP underwriter(s), construction loan administrator(s), and authorized signatory(s) to bind the lender on MAP loan applications.

      2) State that:

         (a) All MAP underwriters have attended MAP Lender training.

         (b) The MAP Lender is currently a HUD approved multifamily mortgagee.

      3) Include corrective actions employed as a result of most recent QC reviews.

      4) Include a summary of loans underwritten by new underwriters (approved within the last fiscal year).

      5) Contain the following language: **WARNING: "HUD will prosecute false claims and statements. Convictions may result in criminal and/or civil penalties. (18 U.S.C. 1001, 1010, 1012; 31U.S.C. 3729, 3802)."**

   c. Submit the certification to:

      US Department of Housing and Urban Development

      Lender Qualification and Monitoring Division (LQMD)

      Office of Multifamily Development

      451 7th Street, SW, Room 6138

      Washington, DC 20410

E. The MAP Lender maintains or has access to the latest **Limited Denial of Participation (LDP)** list available on the Internet at: http://www.hud.gov/offices/enforce/ecldp.cfm.

F. The MAP Lender, for each application, checks the latest **Debarment** list available on the Internet at: http://epls.arnet.gov/.

Note: The Excluded Parties Lists System (EPLS) is the electronic version of the Lists of Parties Excluded from Federal Procurement and Nonprocurement Programs (Lists), which identifies those parties excluded throughout the U.S. Government (unless otherwise noted) from receiving Federal contracts or certain subcontracts and from certain types of Federal financial and nonfinancial assistance and benefits.

G. The MAP Lender does not:

1. Conduct FHA-HUD related business with any person, as defined in 24 CFR 24.105, who are debarred, suspended or subject to a Limited Denial of Participation.

2. Employ or have contact with any individual or firm to perform FHA-HUD related services in origination, processing, and underwriting or construction loan servicing who is restricted from participation in HUD/FHA programs. To this end, the MAP Lender must check their employee list and third party contractors every six months to ensure compliance with this requirement.

H. The MAP Lender retains a copy of the entire case file pertaining to the MAP loan origination, underwriting and/or construction loan administration, either in hard copy or a generally accepted electronic storage format, for example microfilm or scanned and stored on CD Disk, for at least three years from the final endorsement date.

I. The Quality Control Review:

1. Is sufficient in scope to enable the MAP Lender to evaluate the accuracy, validity and completeness of its MAP operation.

2. Provides for independent evaluation of the information gathered or developed by the MAP Lender for use in the MAP origination, underwriting and construction loan administration decision processes.

3. Documents whenever deficiencies in processing, underwriting or construction loan administration are found.

J. Procedures exist for expanding the scope of a QC Review where instances of alleged fraudulent activities or patterns of deficiencies are identified. Other entities or individuals may need to be made part of any ongoing investigation of suspected fraudulent misdeeds to protect their interests as well.

K. The QC Reviewing official(s) defined in Appendix 2C.F above will:

1. Document all findings - positive and negative in writing; and
2. Present each project's QC Review at the next designated committee meeting.

L. Senior management committee meeting.

1. The meeting must be scheduled to meet on a semi-annual basis to hear the findings and recommendations resulting from the QC Reviews or more frequently if serious quality control issues are present.

2. Committee members must receive written notification of deficiencies cited as a result of a QC Review before the meeting.

3. At the meeting, the committee will carefully review and analyze the results of a QC Review and will undertake corrective actions as necessary, including:

   a. Prompt initiation of corrective actions to address all deficiencies, including procedural problems, as identified;
   b. Formal documentation of the corrective actions taken by citing each deficiency, identifying the cause of the deficiency, and providing management's response or actions taken;
   c. Affected third party contractor(s), employees and departments will be notified in writing of such findings, and corrective actions taken to assure senior management that repetitive or recurring actions will not reoccur;
   d. Prompt distribution to all MAP loan origination, underwriting and construction loan administration personnel including contractor(s) of the corrective instructions for the identified deficiencies;
   e. Training for the prevention of such activities will be implemented promptly; and

f. All remedial actions will be re-reviewed for compliance at the next regularly meeting.

M. The MAP Lender reports to LQMD in Washington D.C., and provides the reported results of its QC Reviews (not the entire review with checklists) to include the corresponding corrective action plans, provides assurance that the information being reported is accurate, all required information is being reported, and the information is reported promptly.

The MAP Lender shall promptly notify LQMD of any violation of law or regulation, false statements or program abuses by the MAP Lender, its employees, its contractors or any other party to the transaction. A MAP Lender's Quality Control Program must ensure that findings discovered by employees during the normal course of business and by the quality control staff during reviews/audits of FHA loans are reported to HUD. Findings discovered by employees during the normal course of business and by quality control staff during reviews/audits of FHA loans are reported to HUD within 60 days of the initial discovery. If there is a finding of fraud or other serious violation, finding must be submitted in writing to LQMD. If HUD staff is suspected of involvement, the Lender should refer the matter to the Office of Inspector General, Department of Housing and Urban Development SW, 451 7th Street, Room 8256, Washington, DC 20410.

N. The MAP Lender will retain any QC Review and follow-up, including review finding and actions taken, plus procedural information (such as the percentage of loans reviewed, basis for elected loans, and who performed the review) for a period of three years. These records must be made available to HUD on request.

O. The MAP Lender will periodically review and update the QC Plan.

Specific Requirements of a Quality Control Plan 2E

A. For the MAP Underwriting Function.

1. The QC Plan must address how quality control is integrated into the MAP Lender's **production process**. For example, before they send the AE&C analyst and the appraiser out to do a review they should hold a pre-performance meeting. The pre-performance meeting is an important first step to document how the Lender is enforcing their quality control in the production process. During the pre-performance meeting take attendance, take minutes, record action items, and schedule a follow-up meeting when done. At a minimum the following functions must be met for a thorough review of the QC Plans as it pertains to the production process. The MAP Lender must retain in the loan file all

documentation supporting any determinations of decisions made for these following functions.

2. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining whether the mortgagor is an acceptable credit risk, with a reasonable ability to make payments on the loan obligation.

3. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining that the general contractor, if applicable, is an acceptable credit risk, with a reasonable expectation of completing construction of the project.

4. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining that the property's estimated value, market need, earning capacity, operating expenses, and warranted cost of the property will be sufficiently ascertained to insure that they are sufficient for a long-term HUD insured mortgage.

5. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining that new construction/substantial rehabilitation project's design meets all applicable design standards.

6. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining that project's construction/rehabilitation/repair costs are reasonable.

7. The QC plan must address how the MAP Lender will exercise prudence and due diligence in assuring that they have not established minimum loan amounts, "floors," below which they will not lend. ***Note: This is a violation of Section 535 of the National Housing Act.***

8. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining that they are in compliance with Section 2.6 of the MAP Guide dealing with prohibited identity-of-interest relationships.

9. The QC plan must address how the MAP Lender will exercise prudence and due diligence in assuring that the MAP Lender originators:

   a. Cannot:

(1) Perform the role of underwriter for projects they originate.

(2) Hire contractors on behalf of the underwriter.

(3) ***Small MAP Lenders with limited staff may request a waiver of (1) and (2) above from the Office of Multifamily Development in Washington DC.***

b. Must certify for each loan conflicts-of-interest with the proposed mortgagor or other transaction participants.

10. The QC plan must stipulate that the HUD approved MAP underwriter(s) is(are) a full time employee(s) of the MAP Lender.

11. The QC plan must address how the MAP Lender will exercise prudence and due diligence in assuring that the MAP Lender's technical staff and/or third party contractor(s) are knowledgeable of HUD's requirements. Where required by state or local law or regulation, the technical staff or third party contractor must be properly licensed in the jurisdiction where the project is located.

B. For MAP construction loan administration function.

1. The QC plan must address how the MAP Lender will exercise prudence and due diligence in determining that construction loan administration is performed in accordance with accepted practices of prudent lending institutions and HUD's requirements.

2. The QC plan must stipulate that the HUD approved MAP construction loan administrator(s) is a full time employee of the MAP Lender.

3. The QC Plan must provide for a review of the construction loan administration function in order to:

   - Determine that construction loan administration records are promptly established after loan closing and that the servicing records contain the information necessary to properly service the loan.

   - Determine that inquiries from borrowers concerning their individual loan accounts are promptly responded to.

Submission of Quality Control Plans 2F

The Quality Control (QC) Plan is a required exhibit in the MAP application package. Submit the QC Plan in both paper and electronic formats, e.g. pdf format or Microsoft Word. An authorized signatory of the Lender must sign the original paper document. Whenever the QC Plan is revised the Lender must send updated paper and electronic copies to LQMD.

Quality Control Reviews 2G

Quality Control Reviews (QC Reviews) of the lender's MAP operation are to be performed annually. The annual QC Review shall perform three functions:

1. Track all MAP loans presented by individual loan originators and underwriters.
2. Evaluate the Lender's overall QC plan for adequacy and the lender's operation for compliance to the QC plan
3. Perform audits of individual loan commitments.

A. Tracking: As a function of the annual quality control review, each lender shall track all MAP loans presented by individual loan originators and underwriters.

   a. The term loan originator includes mortgage broker, correspondent or packager.
   b. Annually submit a copy of the tracking report no later than June 30th of each year to:

   US Department of Housing and Urban Development
   Lender Qualifications and Monitoring Division
   Office of Multifamily Development
   451 7th Street SW Room 6138
   Washington, DC 20410

- The first annual tracking report must cover the period from implementation of the MAP procedures forward regardless of where the loan originator or the loan underwriter may have worked.
  - Annual tracking reports for active underwriters include the following information:

    - FHA Number
    - Project Name (identification)
    - Initial/ Final Endorsement Dates
    - Mortgage Insurance Program
    - Original Principle Balance
    - Loan Servicer
    - Loan Status
    - Whether or not the loan has any of the following issues:

      - Waivers
      - Master Lease
      - Underserved Area
      - Criteria 5 (debt service) controlled mortgage Government subsidies (LIHTC, Section 8, etc.)

B. QC Plan Analysis: The annual QC review must evaluate the Lender's overall QC plan for adequacy. It should include an analysis of the lender's operation and for compliance to the QC plan.

   a. The QC review should include an opinion as to whether the lender's QC plan proposes an adequate system to insure that FHA underwriting requirements are followed.
   b. The QC review should include an analysis as to whether or not the lender is following the plan they have proposed.
   c. The QC review should include an analysis as to whether or not the lender has completed the correct number of audit reviews.
   d. The QC review should include an analysis as to whether or not the lender is adequately staffed to implement the QC plan.

C. Audit Reviews:

   1. The QC review shall also include Quality Control (QC) Audit reviews of individual commitments.

a. For MAP Lenders with total commitments on 20 or more loans in the applicable year of review, QC reviews will be completed for 5% of all closed MAP loans. The maximum number of required reviews will be the lesser of 5% of all closed MAP loans or three reviews.

b. MAP Lenders with fewer than 20 commitments in the applicable year of review will be required to perform one QC review.

c. The required number of QC Reviews as defined above will be performed on loans with the greatest Risk Assessment Score as defined herein.

d. Amending previous instructions, MAP Lenders will no longer be required to perform a QC review for each Section of the National Housing Act used.

e. Amending previous instructions, MAP Lenders no longer must perform a QC review for each underwriter, so long as the minimum prescribed number of loans is reviewed.

f. QC audit reviews shall evaluate the quality of work performed by the MAP originators, underwriters and technical staff and/or third party contractor(s). All appraisals reviewed must receive a field review. Field reviews must be performed by qualified senior staff not involved in origination or underwriting; or review appraisers employed on a contract basis. .

g. For QC audit reviews involving new construction/substantial rehabilitation, the QC review should provide an analysis as to whether or not MAP construction loan servicing policies and requirements have been met.

Note: The review appraiser or appraisal firm working on the QC Audit Reviews cannot be used in underwriting any MAP loan.

2. Quality Control Ranking Factors and Review Selection

The QC Review official will assign a risk assessment score to each loan originated in the previous reporting cycle and required audit reviews will be targeted to the loans with the greatest score, concluded to therefore represent the greatest degree of risk to the

Department. Points will be assigned for the following risk indicators:

- Loans that are troubled, defaulted, or assigned:	20 Points
- Mortgage amount over $15,000,000:	15 Points
- Mortgage amount over $10,000,000:	10 Points
- Mortgage amount over $5,000,000:	5 Points
- Mortgage amount over $1,000,000:	1 Point
- New Construction Loans:	15 Points
- Substantial Rehabilitation Loans:	10 Points
- Purchase Loans:	5 Points
- Refinance Loans:	1 Point
- Loans that are not typical in size (small numbers of units or high numbers of units):	5 Points
- Loans in which Criterion 5, Debt Service, established the Maximum Loan Amount:	5 Points
- Loans underwritten by underwriters approved within the last three years:	10 Points
- Loans underwritten by underwriters with a default in the previous three reporting cycles:	10 Points
- Loans that have waivers:	5 Points
- Loans in underserved areas:	5 Points
- Unsubsidized loans	5 Points
- Properties with a Master Lease:	10 Points

3. Audit Reviews of Problem Loans.

   In addition to the above review requirements, the originating MAP Lender must also undertake a comprehensive review and reexamination of any MAP loan it underwrote that goes into default either during construction or within ***three years*** after final endorsement. This must be done in all cases including those in which the MAP Lender no longer has the loan in its portfolio.

4. Loans purchased/transferred from another MAP Lender.

   While not required, we encourage MAP Lenders to perform basic due diligence QC Review on any loan purchased from another MAP Lender.

Specific Requirements For Quality Control Audit Reviews

2H

The purpose of individual loan audit reviews is to determine the accuracy and completeness of underwriting conclusions and MAP Lender documentation. At a minimum, the following requirements must be met for QC Reviews of loans underwritten using the MAP procedures.

A. All processing and underwriting must comply with the applicable provisions of the NHA, Title 24 of the Code of Federal Regulations, the MAP Guide, the MAP Forms Book and MAP FAQs.

B. All identity-of-interest certifications were properly filed.

C. Determine whether each loan file contains all HUD required loan processing, underwriting and legal documents including supporting reports and that all required documents were provided to HUD.

D. Determine if there was a violation of the Department's prohibition of referral fees.

E. Determine if anything of value was paid directly or indirectly to any person or entity who has received any other compensation from the mortgagor, seller, builder, or any other person for services related to the transaction, or related to the purchase or sale of the mortgaged property. Exception can be made where services were actually rendered, the name of the broker is furnished, and there is no identity of interest between the mortgagee and the broker or the mortgagor and the broker, and the Hub Director has given her or his approval in writing. The broker's fee must be included on the Mortgagee Certificate.

F. Determine if staff allowed third parties to represent the MAP Lender in meeting(s) with the Hub/Program Center to discuss specific MAP projects.

G. Determine if excess and unallowable fees are being charged to mortgagors. Examples include charging discount points not disclosed on the Mortgagee's Certificate, Form HUD-2434, or at firm commitment, charging larger fees than permitted by HUD/FHA.

H. If new construction or substantial rehabilitation, did the pre-application submission include

an acceptable narrative summary, summarizing the market study and extent of competition as well as describe the features of the proposal which may present problems, such as zoning, ground leases, and environmental issues.

I. Did the Lender's pre-application submission list the proposed MAP Lender reviewers? Were any proposed reviewers rejected by the Hub, and, if so, why?

J. In the application for the firm commitment, did the Lender provide a narrative analysis which discussed the characteristics of the project for which mortgage insurance was sought, presenting the reasons that the Lender recommends the loan for mortgage insurance?

K. Did the Lender's narrative analysis for the firm commitment application discuss the risk factors?

L. Did the narrative analysis for the firm commitment application properly evaluate the financial capacity and the experience in multifamily housing of the principals of the borrower?

M. If the application is for refinancing or purchase, did the narrative analysis provide a satisfactory description of the property?

N. Did the Lender's narrative analyses provide a satisfactory analysis of the market, the rents, and expenses, and the estimated rent-up costs and operating deficit?

O. For refinancing, did the Lender determine the adequacy of the reserve for replacement?

P. Did the underwriter make any changes to the appraisal or technical reports? If so, what were they, what was the justification?

Q. At the Lender's request, did the Hub or Program Center Director waive any of the MAP requirements? If so, what requirements were waived and were there justification for the waivers?

R. At the Lender's request, were any waivers requested by the Hub Director from HUD Headquarters? If so, what were the waivers requested, and was the request approved or rejected and why?

S. Did the Lender obtain the necessary certifications from the individual reviewers?

T. Did the Lender certify that the proposed loan represented an acceptable risk to the Department (Section 220, or 221d3, 221d4 or 231) or is economically sound (Section 223(f)), based upon the Lender's analysis, and that the loan complied with all FHA statutory, regulatory and administrative requirements?

U. Did the Lender prepare a Master HUD 92264 signed by the Lender's underwriter?

V. Did the Lender submit an application for a firm commitment within 120 days of the date of the invitation letter? If not, did it request an extension, providing justification for the extension request?

W. Were any changes made by the underwriter to a technical report's finding, conclusions and/or recommendations? If so, was it documented fully and supported by data.

X. Credit reports on businesses and individuals.

   a. Determine whether the loan file contains business and individual credit report(s) on the appropriate principals, sponsor, mortgagor, and general contractor, if applicable.
   b. Determine if more than one credit report was ordered on the same principal/company; and if so, whether the most current credit reports were submitted with the loan package to HUD-FHA.
   c. Determine whether any outstanding judgments shown on the credit report(s) were accompanied by an explanation and supporting documentation. If delinquent Federal debt existed, the Lender must have included a letter from the Federal agency in accordance with Section 8.3G of the MAP Guide.

Y. Determine whether verifications of deposit and trade references were sent, received and considered in the project underwriting.

Z. Determine whether all conflicting information or discrepancies were reconciled and properly documented in writing.

AA. Determine that the loan file contains a financial statement(s) on the principals, sponsor, and on the mortgagor. If the project involved new construction or substantial rehabilitation, determine if a financial statement was obtained from the general contractor.

BB. Determine that the financial statements were analyzed following generally accepted business practices to determine financial capability.

CC. Verify that the MAP underwriter determined that the sponsor and/or general contractor had a sufficient level of experience for the type and/or size of project that was approved.

DD. Determine if all negative information about the project and individuals or entities involved in the transaction was disclosed to HUD in the underwriter's written summary.

EE. Determine if the underwriter performed due diligence quality control over the work of the MAP Lender's staff and/or third party contractors used in underwriting the project.

a. Determine if the preparers of the forms/reports/reviews are qualified as required by the MAP guide, and have insurance, if the MAP Guide requires any.

b. Determine if the forms/reports/reviews were prepared in the manner required by the MAP Guide and that the forms/reports/reviews are complete and accurate.

c. Determine if the proposed loan represents an acceptable risk based on the underwriters review and analysis.

d. Determine if the required reports and documentation flowed in a timely manner from one discipline to another.

FF. Determine that the underwriter analyzed the project's proposed management program. This includes a review of the management agent's past experience and performance to determine the agent's capacity and track record to assure that the development should be managed in a prudent, efficient and cost effective manner.

GG. Determine if the underwriter verified the professional used in the environmental review and selected by the sponsor/developer was qualified for the assigned responsibilities.

HH. Determine if the underwriter provided HUD with a narrative report and supporting documentation plus the Phase I Environmental Site Assessment (ESA) or Phase II ESA.

QC Reviews - Appraisal Review 2H .1

For the appraisal review portion of the QC Review:

A. Determine if the appraiser was properly certified in the appropriate jurisdiction. (Temporary certifications may be acceptable so long as the appraiser meets all competency requirements).

B. Provide the review appraiser's opinion as to the completeness of the material under review.

C. For Section 220, 221(d) or 231 appraisal processing:

1. Does the appraiser meet the qualification and competence requirements outlined in the MAP Guide?

2. Is the appraisal a narrative self-contained report that is inclusive of and supportive of all required HUD Form Documentation (HUD-92264, HUD-92264-A, HUD-92273 and HUD-92274)?

3. Does the appraisal have an effective date within 120 days before the date of firm commitment?

4. Does the appraisal include the appraiser's USPAP required certification?

5. Did the primary appraiser designated by the lender and approved by HUD perform the property inspection and sign the appraisal report and supporting form documentation?

6. Did the appraisal include photographs of the subject, the comparable sales and comparable rentals?

7. Does the appraisal adequately describe and analyze the geographic area, neighborhood, rental competition, sales comparables, the site and the subject improvements?

8. Does the appraisal establish the project's "Replacement Cost" in accordance with Chapter 7, Section 7.4 of the MAP Guide, and Form HUD-92264 instructions?

9. Substantial Rehabilitation – Does the appraisal include a supplemental HUD 92264 that identifies the "As Is" Value of the improvements, supported by the income and direct sales comparison approaches, as defined in HUD Handbook 4465.1 and the MAP Guide?

10. New Construction – Does the appraisal identify the "Warranted Price of Land" as defined in HUD Handbook 4465.1 and the MAP Guide?

11. Does the appraisal identify the "Estimate of Market Rent by Comparison," as of the appraisal date, arrayed in the included HUD-92273 and as defined in the Form's instructions?

12. Does the appraisals identify the project's estimated potential gross income and stabilized occupancy ratio in the included HUD-92264 and defined in the Form's instructions?

13. If commercial facilities are located within the project, does the appraisal include a separate analysis of the effect the commercial space will have on the project, as outlined in the MAP Guide; and does the commercial space meet the income and floor area limitations outlined in the MAP Guide?

14. If any comparables have rent concessions, did the appraisal account for them in the market rental analysis as defined in the MAP Guide?

15. Does the appraisal identify the project's estimated operating expenses, based upon at least three expenses comparables arrayed in the included HUD-92274, and as defined in the Form's instructions?

16. Does the appraisal properly update the expense comparables, meet disclosure requirements for the comparables, and has the subject property's expenses been updated to the date of the appraisal per Form HUD 92274 instructions?

17. Does the appraisal identify the estimated operating deficit and replacement reserve requirements, as defined and outlined in the MAP Guide?

18. Does the appraisal provide an estimation of the maximum insurable mortgage by completing a Trial Form HUD-92264-A?

D. For Section 223(f) appraisal processing:

1. Does the appraiser meet the qualification and competence requirements outlined in the MAP Guide?

2. Is the appraisal a narrative self-contained report that is inclusive of and supportive of all required HUD Form Documentation (HUD-92264, HUD-92264-A, HUD-92273 and HUD-92274)?

3. Does the appraisal have an effective date within 120 days before the date of the submission of the application for a firm commitment?

4. Does the appraisal include the appraiser's USPAP certification?

5. Did the primary appraiser designated by the lender and approved by HUD perform the property inspection and sign the appraisal report and supporting form documentation?

6. Did the appraisal include photographs of the subject, the comparable sales and comparable rentals?

7. Does the appraisal adequately describe and analyze the geographic area, neighborhood, rental competition, sales comparables, the site and the subject improvements?

8. Does the appraisal establish the project's fair market value supported by reconciliation of the cost, income and sales comparison approaches in accordance with Chapter 7, Section 7.4 of the MAP Guide and Form HUD-92264 instructions?

9. Does the appraisal establish a total estimated replacement cost and apply all applicable forms of depreciation for use in the final reconciliation process?

10. Does the appraisal identify the "Warranted Price of Land" as defined in HUD Handbook 4465.1 and the MAP Guide?

11. Does the appraisal identify the "Estimate of Market Rent by Comparison," as of the appraisal date, arrayed in the included HUD-92273 and as defined in the Form's instructions?

12. Does the appraisal include the current rent roll, a statement of current occupancy and does it identify the project's estimated potential gross income and stabilized occupancy ratio in the included HUD-92264 and defined in the Form's instructions?

13. If commercial facilities are located within the project, does the appraisal include a separate analysis of the effect the commercial space will have on the project, as outlined in the MAP Guide; and does the commercial space meet the income and floor area limitations outlined in the MAP Guide?

14. If any comparables have rent concessions, did the appraisal account for them in the market rental analysis as defined in the MAP Guide?

15. Does the appraisal present at least three years of historic expenses, and have the forecasted expenses been based upon the historic operation of the property supported by at least three expense comparables arrayed in the included HUD-92274, and as defined in the Form's instructions?

16. Does the appraisal properly update the expense comparables, meet disclosure requirements for the comparables, and has the subject property's expenses been updated to the date of the appraisal per Form HUD-92274 instructions?

17. If it is applicable, does the appraisal identify the estimated operating deficit and replacement reserve requirements, as defined and outlined in the MAP Guide.

18. Does the appraisal provide an estimation of the maximum insurable mortgage by completing a Trial Form HUD-92264-A?

QC Reviews - Market Study Review

2H .2

For the Market Study review, the review appraiser should provide his opinion as to the completeness of the material under review, and determination of overall compliance with market study processing requirements:

A. Does the market analyst meet the qualification and competence requirements outlined in the MAP Guide?

B. Is the market study a narrative self-contained report?

C. Does the market study have an effective date within 120 days before the date of submission of the pre-application, or, with refinancing, within 120 days of submission of the application for a firm commitment?

D. Does the market study adequately describe and analyze the geographic boundaries and general characteristics of the market area, specific market conditions, characteristics of projects under construction and in the planning stages, and contain a supply and demand estimate and analysis and estimated absorption time (if applicable)?

E. Is the market study prepared in accordance with the information supplied by the MAP lender described in Appendix 4 of the MAP Guide?

F. Is the market study prepared in accordance with the format prescribed in the appropriate MAP Guide Appendix?

G. Does the market study include the market analyst's certification?

H. Review appraiser's opinion as to the adequacy and relevance of the data and the propriety of any adjustments to the data.

I. Review appraiser's opinion as to the appropriateness of the analysis methods and techniques used.

J. Review appraiser's opinion as to the analyses, opinions, and conclusions.

QC Reviews - Architectural Review 2H. 3

A. For the Architectural portion of the QC Review of audits of Sections 220, 221(d) or 231, Lender's Architectural Analyst Review Report:

1. Has the Architectural Analyst determined that the Mortgagor's Architect (or other persons or organizations providing architectural services) is qualified to provide the design services to the project and to administer the construction contract?
2. Owner-Architect Agreement (AIA Document B108). (Indicate if separate Agreements are required for design and construction services.)

   a. Are all necessary services included without deletion?
   b. Is compensation other than fixed fee?

3. Architectural Standards. Does the Lender's Architectural Analyst review report address:

   a. HUD Minimum Property Standards
   b. Applicable Building Codes
   c. Accessibility Laws:
      - Fair Housing Act
      - UFAS (if Part 504 is applicable)
   d. Energy Efficiency

4. Does the report address the mortgagor's A&E exhibits?

   a. Are drawings and specs complete and correct?
   b. Is utility service available?

5. Experience and qualifications of general contractor:

a. Did the Lender's architectural analyst prepare a written review of the general contractor?
b. Does the review indicate acceptance?

6. Identity of Interest review: Did the Lender's architectural analyst perform an Identity of Interest review as described here below?

   a. Is there a description of any and all identities of interests that exist between the owner's architect or engineer, the owner, and the general contractor?
   b. Is there a description of any and all identities of interest that exist between the general contractor, subcontractor(s) and material supplier(s)?

   c. If no identities of interest exist, is this stated?

7. Site visit: Does report address:

   a. Physical features (existing construction, topography, drainage, etc).
   b. Unusual site conditions, demolition, offsite construction.
   c. Environmental conditions/hazards.

8. Establish an Architectural Liaison with the mortgagor's Architect:

   a. Is there a processing record of architectural/engineering actions?
   b. Is there an acceptable journal of architectural actions?
   c. Is there an organized file of HUD applications, forms, and documents?
   d. Is there a record of meetings and contacts with the mortgagor's Architect?
   e. Is there clear documentation?

9. Liaison with HUD labor relation staff:
   Did the liaison verify the applicable Davis-Bacon wage rates?

10. Establish a liaison with Lender's cost analyst:

11. Review of Firm Commitment architectural/engineering exhibits:

a. Is there a clear and complete exhibit review list?

b. Is there a statement indicating that:

(i). Firm Commitment architectural exhibits are acceptable without condition, and

(ii) All deficiencies have been acceptably corrected?

c. Does report address:

(i) Completeness of contract documents

(ii) Conformance to local building codes and HUD standards

(iii) Accessibility for persons with disabilities

(iv) Site design

(v) Building design

12. Preparation of architectural portions of Form HUD-92264:

a. Is there a Form HUD-92264 with all architectural portions complete?

- Section A – Architectural portions
- Section B - Architectural portions
- Section C - Unit breakdown with net areas
- Section D - Architectural portions

b. Has the architectural analyst signed the form?

13. Report to the Lender's Underwriter:

a. Has the architectural analyst submitted a report on the project to the Lender's underwriter?

b. Does the report contain an analysis of the project?

c. Does the report recommend:

Acceptance

Negotiated changes with the mortgagor

Rejection

14. Standard Certification:

    Did the Lender's architectural analyst submit a Standard Certification (MAP Section 11.2.M)?

15. Mortgagor's Architect's Certification:

    Is there a Design Architect's Certification (MAP Appendix 5N)?

16. Substantial Rehabilitation projects:
    a. Has the Lender's architectural analyst submitted a report of the Joint Inspection?
    b. Does the report indicate that a complete and thorough inspection was conducted?
        On all features of the project site
        On sufficient living units
    c. Has the Lender's architectural analyst prepared a report on the mortgagor's Architect's Detail Work Write-up?
    d. Does the report address:
        All general work requirements?
        Specific work requirements?
        Clarity or vagueness of work requirements?
        Historic requirements?
    e. Has the Lender's architectural analyst indicated whether there are engineering Reports?
    f. Has mortgagor been notified of requirements?
    g. Has exact nature of engineering report been covered?
    h. Any special tests?
    i. Seismic resistance in applicable seismic zones?

B. Sections 223(f) - Lender's Architectural Analyst review report:

1. Liaison with Lender's cost analyst:
   Is there documentation of contacts regarding:

- Nature and cost of repairs?
- Replacement reserve items?

2. Lender review of Project Capital Needs Assessment (PCNA):

   a. Does Physical Inspection Report (PIR) address:
      - Adequacy of number of dwelling units inspected
      - Condition of project
      - Repair Work Write-up
        - Critical repairs
        - Non-critical repairs
      - Expected component replacement and major maintenance needs
        - Near Term
        - Long Term
        - Remainder
      - Compliance with accessibility laws (for projects built after 3/13/1991)?

   b. Does Statement of Resources and Needs address:
      - Review and possible adjustment to the PIR
      - Identification of Critical and Non-Critical Repairs

   c. Is there evidence that all Critical Repairs have been adequately completed and inspected?

3. Review of mortgagor's exhibits:
   - Has Lender's architectural analyst prepared a review report of mortgagor's exhibits?
   - Does report indicate whether exhibits are complete and correct?

4. Preparation of architectural portions of Form HUD-92264:

   a. Is there a Form HUD-92264 with all architectural portions complete?:
      - Section A – Architectural portions
      - Section B - Architectural portions

- Section C - Unit breakdown with net areas
- Section D - Architectural portions

b. Has the architectural analyst signed the form?

5. Report to the Lender's Underwriter:

   a. Has the architectural analyst submitted a report on the project to the Lender's underwriter?
   b. Does the report contain an analysis of the project?
   c. Does the report recommend:
      - Acceptance
      - Negotiated changes with the mortgagor
      - Rejection

6. Standard Certification:

   Has the Lender's architectural analyst submitted a Standard Certification (MAP Section 11.2. I)

QC Reviews – Cost Review 2H. 4

A. For the Cost Review of Sections 220, 221(d) or 231 - Lender's Cost Analyst review report:

1. Did the Lender hire a qualified construction cost estimator with experience in multifamily cost estimating?

2. A detailed independent cost estimate must provide:

   a. Documentation of the method of estimation and data source.
   b. To be summarized on Form HUD-92326:

- Detailed structure(s) and land improvement cost estimates, and costs of unusual site development
- Contractor's General Requirements
- Contractor's General Overhead
- Contractor's Profit (for non-BSPRA cases)
- Architect's Design and Supervision fees
- Bond Premium and Mortgagor's and Contractor's
- Other Fees
- Onsite demolition costs
- Offsite improvements costs
- Project's Cost Not Attributable (CNA) to dwelling use
- For sub rehab projects, complete Rehab CNA Worksheet (MAP Appendix 6C).

3. Preparation of cost portions of Form HUD-92264:

   a. Is there a Form HUD-92264 with all cost portions completed?
      - Section G – Cost portions
      - Section M
   b. Has the cost analyst signed the form?

4. Review of Form HUD-2328, Contractor's and/or Mortgagor's Cost Breakdown:

   a. Is HUD-2328 complete and signed by all parties?
   b. Has Lender's cost reviewer prepared a comparison of Form HUD-2328 and the independent cost estimate on Form HUD-92326?
      - Line item comparison on Form FHA-2331-B
      - Written documentation of resolution of significant differences in
      - Lender's HUD-92326 and contractor's HUD-2328 cost estimates.
      - Has Lender's cost reviewer prepared a written recommendation of approval or disapproval of contractor's HUD-2328?

5. Property Insurance Schedule, Form HUD-92329:

a. Has the Lender's cost analyst prepared and signed Form HUD-92329?
b. Is there a backup worksheet indicating how the Insurable Value(s) of the project structure(s) were determined?

6. Identity of Interest Review:

a. Has Lender's cost reviewer been supplied with Identity of Interest information by Lender's architectural reviewer?
b. For an identified general contractor:
   - Does the cost estimate indicate "BSPRA" under Builder's Profit?
   - Has the 50-75% rule been applied to determine whether the contractor qualifies for general overhead and profit or BSPRA, or should it be replaced by the dominant subcontractor?
c. For Identified subcontractors and/or material suppliers:
   - Is there documentation that the Identity of Interest subcontract(s) were submitted for prior approval of overhead and profit?
   - If any subcontract(s) were not submitted, has overhead and profit been deleted from the accepted contract amount?
   - Have letter(s) of approval/disapproval been prepared for the mortgagor and general contractor?

7. Report to Lender's underwriter:

a. Has the cost analyst submitted a report on the project to the Lender's underwriter?
b. Did the report contain an analysis of the project costs?
c. Did the report recommend?
   - Acceptance
   - Negotiated changes with the mortgagor
   - Rejection

8. Standard Certification:

a. Did the Lender's cost analyst submit a Standard Certification (MAP Section 11.2.M)?

9. Substantial Rehabilitation projects:

   a. Joint Inspection Report and Architect's Detail Work Write-up:
      - Does the Lender's cost analyst have a copy of the Joint Inspection report?
      - Does the Lender's cost analyst have a copy of the mortgagor's Architect's Detail Work Write-up?
      - Do the Joint Inspection Report and Architect's Detail Work Write-up include Reserve for Replacement (R4R) items?
        - Is there an itemized breakdown of R4R items?
        - Does the breakdown indicate the age and remaining useful life of the R4R items?

   b. Detailed Cost Estimate:

      Does the Lender's cost analyst's detail cost estimate clearly reflect all the scope of work items in the Detail Work Write-up?

   c. Reserve for Replacement estimate:
      - Has the Lender's cost analyst provided an R4R cost estimate?
      - Is the R4R cost estimate itemized and incorporate the remaining useful life for the R4R items?
      - Is there a replacement schedule for the R4R items?

B. Sections 223(f):

1. Qualifications of Lender's Cost Analyst and Needs Assessor are acceptable?

2. Liaison with Lender's architectural analyst:

   Is there documentation of contacts regarding the PCNA?

3. Summary of cost estimate for hypothetical "as new" building:

   a. Documentation of method of estimation and data source.

   b. Summary "bottom-line" cost estimate:
      - Structure(s) and land improvement cost estimates, for hypothetical "as new" building:
      - Contractor's General Requirements
      - Contractor's General Overhead

- Contractor's Profit
- Architect's Design and Supervision fees
- Bond Premium and Mortgagor's and Contractor's Other Fees

4. Preparation of cost portions of Form HUD-92264:
   a. Is there a Form HUD-92264 with all cost portions complete?
      - Section G – Cost portions (hypothetical "as new" costs)
      - Section M must be blank.
      - Are Critical Repair costs and Non-Critical Repair costs summarized in Section O?
   b. Has the cost analyst signed the form?

5. Review of Project Capital Needs Assessment (PCNA). Did the Lender's cost analyst prepare a written report reviewing:
   a. Cost portions of Project Inspection Report (PIR):
      - Cost of Critical repairs
      - Cost of Non-critical repairs

      For all deferred non-critical repairs, estimate the required escrow amount.

   b. Expected cost of expected component replacement and major maintenance needs for:
      - Near term
      - Long term
      - Remainder
   c. Statement of Resources and Needs recommending:
      - Initial Deposit to the Reserve for Replacement, if any
      - Annual (or monthly) deposit to the Reserve for Replacement
      - Near Term replacement schedule indicating annual deposits, itemized expenditures, and remaining funds at the end of each year.

6. Documented advice to Lender concerning the PCNA:

   Lender's cost analyst must provide opinions and recommendations for acceptance or change to PCNA regarding cost items:
      - Critical and Non-critical repairs
      - Funding schedules in Near Term, Long Term and Remainder items in

the Reserve for Replacement account

7. Property Insurance Schedule, Form HUD-92329:
   a. Has the Lender's cost analyst prepared and signed Form HUD-92329?
   c. Is there a backup worksheet indicating how the Insurable Value(s) of the project structure(s) were determined?

8. Report to Lender's underwriter:
   a. Did the cost analyst submit a report on the project to the Lender's underwriter?
   b. Does the report contain an analysis of the PCNA?
   c. Does the report recommend?
      - Acceptance
      - Negotiated changes with the mortgagor
      - Rejection

9. Standard Certification:
   Has the Lender's cost analyst submitted a Standard Certification (MAP Section 11.2. I)

Quality Control Review Requirements for Construction Loan Administration

2I

The QC Review of construction loan administration must, at a minimum, meet the following requirements.

A. Analyze loans for general compliance with HUD-FHA construction loan administration requirements found in the MAP Guide, the MAP Forms Book, and MAP Frequently Asked Questions.

B. Analyze escrow administration to assure that the escrows are properly funded and that the funds are only used for their intended purposes.

C. Analyze procedures for collection and recordation of payment receipts; escrow bills; disbursements from escrow; and claim submissions.

D. Analyze procedures that were use for handling letters-of credit.

E. Analyze procedures that were use for handling the investment of construction loan escrows.

F. Analyze the procedures for processing construction loan advances, change orders and notification of surety, cost certifications, and post endorsement escrows.

G. Analyze delinquent loans and loans in foreclosure to determine compliance with HUD-FHA fiscal requirements and procedures such as timely assignments and extension requests, property preservation requirements and inspections.

H. Review claim submissions on projects that have not reached final endorsement to assure that all efforts have been exhausted to "work-out" the loan and that all claims are properly documented, supported, and filed in accordance with HUD-FHA requirements.

Independence of Quality Control Reviews 2J

A. The Quality Control function must be independent of the origination and servicing functions. This independence may be accomplished in a number of ways. Quality control functions may be performed by using:

1. **In-house staff.** Lenders may establish a unit that is dedicated solely to Quality Control. Staff performing Quality Control must not be involved in the day-to-day Processes that they are reviewing.
2. **Outside firms.** MAP Lenders may use knowledgeable outside independent firms to assist in the performance of the QC Reviews.

B. The outside source must use the MAP Lender's QC Plan in completion of the annual QC review.

C. Services provided by an outside firm must comply with the Department's quality control requirements, and must provide written reports to the MAP Lender's senior management. The MAP Lender will be responsible for ensuring these requirements are met.

D. The firm working on the QC Reviews cannot be used in underwriting MAP loans.

E. Certified Public Accounting (CPA) firms may work on the QC Review. This would be considered non-audit services. However, the same CPA firm cannot provide auditing services for that MAP Lender based on Government Auditing Standards, issued by the U.S. General Accounting Office, since the CPA firm will be reviewing its own work in part, which is a violation of the Independence standard of the Auditing Standards.

F. Any agreement with the outside firm must be in writing, state the roles and responsibilities of each party, and be available for review by HUD staff.

Events Leading to Change in MAP Participation Status 2K

A. To maintain its MAP eligibility, the Lender must comply with its QC Plan and the underwriting, monitoring and servicing requirements of MAP on a continuous basis.

B. Failure to comply with these requirements may result in revocation of MAP privileges and/or other administrative sanctions.

Appendix 4

Application Requirements Checklist
Table of Contents

	Title
4A	Sections 220, 221(d)(3), 221(d)(4) and 231 New Construction and Substantial Rehabilitation
4B	Section 223(f) for Refinance or Purchase of Existing Apartments
4C	Sample MAP Invitation Letter Format
4D	Firm Commitment Special Conditions

THESE APPENDICES CONTAIN THE CHECKLISTS THAT INCLUDE FORMS AND DOCUMENTATION OF EXHIBITS THAT ARE REQUIRED FOR AN APPLICANT TO SUBMIT A LOAN PACKAGE FOR MORTGAGE INSURANCE.

HOWEVER, THERE ARE SOME EXHIBITS THAT ARE TOO DETAILED FOR INCLUSION ON THESE CHECKLISTS LISTS, AND THERE ARE DOCUMENTS REQUIRED BY THE GUIDE TEXT THAT MAY IN SOME CASES NOT BE MENTIONED HERE, BUT, RATHER ARE REFERENCED IN THE MAP GUIDE CHAPTERS.

IN SUCH CASES, THE EXHIBTS AND DOCUMENTS REQUIRED BY THE GUIDE TEXT AND THE EXHIBITS ON THESE CHECKLISTS ARE STILL SUBMISSION REQUIREMENTS.

New Construction and Substantial Rehabilitation - Sections 220, 221(d)(3), 221(d)(4), and 231

4A

I. PROJECT CONCEPT MEETINGS

All projects (both market rate and affordable) must participate in a concept meeting with the program center, either in person or by teleconference, where the project has an early review before submitting a pre-application or direct to Firm application. The exhibits required for the concept meeting for New Construction and Substantial Rehabilitation Proposals are the following:

1. Section of the Act
2. Number of market rate and affordable units
3. Projected mortgage amount
4. Basic information on developer and principals
5. Management company
6. General contractor
7. Previous HUD experience
8. Geographic location with map
9. Photographs of the subject and immediate surroundings
10. Site improvements (existing/proposed)
11. Commercial component – discuss potential residents
12. Amenities
13. Community / city / state support
14. Green / sustainability Issues
15. Development status (e.g., have any permits/approvals been obtained?)
16. Discuss general market conditions, competitive properties and comparables
17. Environmental issues
18. Potential risks and mitigating factors
19. Any anticipated waiver requests

II. PRE-APPLICATION

Résumés of Lender's underwriter, appraiser, and/or market analyst if not submitted prior to the pre-application.

III. PRE-APPLICATION

A. Exhibits Required for the Pre-application Review

1. Narrative Description of Proposed Project.
2. Form HUD-92013, "Application for Multifamily Housing Project," including the developer's summary cost figures.
3. Form HUD 92013-E, Supplemental Application and Processing Form (Housing for the Elderly/Disabled)
4. Application fee for market rate pre-applications, a non-refundable 15 basis point fee.

5. Preliminary sketch plans, consisting of:
   a. Site plan.
   b. Typical unit and building layouts.
   c. Ground floor and typical floor plans.
   d. Wall section plan.
6. Market Study with comparables, commercial income analysis
7. Appraisal Exhibits. Forms HUD-92273, HUD-92274 and HUD-92264T (if applicable), dated no more than 120 days before the date of the pre-application package submission. If the processing calls for tax credit and/or bond financed applications, a HUD-92264T must also be included.
8. Photograph(s) of the property and immediate area.
9. Evidence of site control.
10. Location map or maps.
11. If commercial space involved, show estimated percentage of total square feet and estimated total income.
12. If pre-application is under Section 220, evidence that property is in eligible area.
13. Copy of ground lease (207 Lease Addenda), if any.
14. Phase I Environmental Site Assessment with a narrative environmental report; a Phase II, if applicable.
15. Marketing, Leasing, and (if applicable) Relocation Plan.
16. If state or local government grants or loans are anticipated as part of the project, evidence that such funds will be available. If tax credits (e.g. LIHTC, Historical and New Market) are anticipated provide a certification.
17. Résumés showing experience of owners/sponsor and key principals.
18. If Sponsor is nonprofit, Form HUD-3433, "Request for Preliminary Determination as a Nonprofit Sponsor and/or Mortgagor" and supporting documents.
19. If Sponsor is non-profit, Developer's Agreement or another document showing relationships and work responsibilities of all parties associated with the transaction.
20. Active Partner Performance System Participate Certification – Electronic or Paper 2530 are acceptable. Also applies to lessees.
21. Disc or removable drive of the underwriting file, exhibits and third party reports.

B. Additional Exhibits at Pre-Application for Substantial Rehabilitation.
   1. "As is" sketch plans in addition to preliminary sketch plans listed in 9, above.
   2. Mortgagor's architect's basic work write-up, including summary cost estimates of major trade item groups if a partial (non-gut) rehabilitation.
   3. Lead-based paint and asbestos test reports for projects constructed prior to 1978.
   4. Plans for relocation of existing residents affected by work.

5. Appraisal Exhibits. Forms HUD-92273, HUD-92274 and HUD-92264T (if applicable), dated no more than 120 days before the date of the pre-application package submission. If the processing calls for tax credit and/or bond financed applications, a HUD-92264T must also be included.
6. Property financial statements on the past three years.

III. APPLICATION FOR FIRM COMMITMENT

A. Exhibits Required for Firm Commitment Applications. Make any changes necessary in the pre-application exhibits and resubmit any exhibit that is changed. In addition to pre-application submit the following for a complete package:

1. Transmittal letter.
2. Application for Multifamily Housing Project (Form HUD-92013) with fee of $3 per $1000 (30 basis points) of mortgage; or the balance of the market rate pre-application fee, 15 basis point.
3. Form HUD 92013-E, Supplemental Application and Processing Form (Housing for the Elderly/Disabled)
4. Narrative Summary and Underwriter's Recommendation.
5. Intergovernmental review. See HUD Processing Office to determine State Single Point of Contact and whether review is required for state where property is located.
6. Byrd Amendment (Lobbying Certification and disclosure). See 24 CFR Part 87.
7. Completed Form HUD-92264 Multifamily Summary Appraisal Report with technical analysis and standard certifications by all Lender third party analysts.
8. Form HUD 92264-A Supplement to Project Analysis.
9. Active Partner Performance System Participate Certification - Electronic or Paper 2530 are acceptable, if not submitted at Pre-Application.
10. Verification of social security or employer identification number.
11. Site control document (sales contract).
12. Affirmative Fair Housing Marketing Plan, Form HUD-935.2A. (See Handbook 4350.3 REV-1)
13. Equal Employment Opportunity Certification.
14. Certification from Mortgagor's Architect.
15. Report prepared by Lender's architectural analyst.
16. Résumés of Lender's architectural reviewer and cost reviewer, if not submitted prior to the application.
17. Owner-Architect Agreement on AIA Document B108 and HUD Amendment.
18. Legal Survey Form HUD-92457, Surveyors Report. (Initial Endorsement)

19. Engineering and specialty reports, if not covered under environmental report.
20. Contract drawings and specifications.
21. Municipal services and other utilities' assurance letters.
22. Off-site improvements/construction (description).
23. Cost estimate package, Form HUD-92264.
24. Contractor's and/or Mortgagor's Cost Breakdown, Form HUD-2328.
25. Property Insurance Schedule, Form HUD-92329.
26. Identity of Interest disclosure and the 50-75 percent rule disclosure.
27. Résumé of the general contractor and Schedule of jobs (work) in progress.
28. Soils report and foundation analysis.
29. Appraisal with all supporting documents:
    a. Rental Housing Income Analysis and Appraisal, Form HUD-92264
    b. Estimates of Market Rent by Comparison Form HUD-92273
    c. Operating Expense Analysis Worksheet Form HUD-92274
30. Phase I Environmental Site Assessment with a narrative environmental report, if updated from report submitted at pre-application; a Phase II, if applicable.
31. Marketing, Leasing, and (if applicable) Relocation Plan, if updated from pre-application.
32. Evidence of last arms-length transaction and price.
33. Personal Financial and Credit Statement, Form HUD-92417.
34. Financial Statements for Business Entities, Schedule of Real Estate Owned; Schedule of Mortgage Debt, if applicable.
35. Credit reports current within 30 days of the application date.
36. Form HUD-92013 - Supplement for Sponsor, mortgagor, each principal of the mortgagor and general contractor and disclosure of prior legal action relevant to mortgage financing, outstanding delinquent Federal Debt.
37. Requests for verification of deposits for each bank reference included on Form HUD-92013 Supp.
38. Certification approving release of banking and credit information.
39. If relevant, tax credit certification(s), i.e. LIHTC, Historic, New Market.
40. If supplemental grants and/or loans are part of project financing, provide commitment letter.
41. Financing plan (sources and uses statement for tax credit projects).
42. Organizational documents creating mortgagor entity, if applicable.
43. If Sponsor is nonprofit, Developer's Agreement (if not submitted at pre-application).
44. Form HUD-3434, Certificate of Relationships and nonprofit motives, and Form HUD-3435, Certificate of Contractual Relationship.
45. HUD-2238, Financial Requirements for Closing.

46. Résumé of management agent.
47. Form HUD-9839 A, B, or C, Management Certification.
48. Form HUD-9832 Management Entity.
49. Management Plan and Sample Lease.
50. Management Agreement, if any.
51. Disc or removable drive of the underwriting file, exhibits and third party reports.

B. Additional Substantial Rehabilitation Exhibits for Firm Application

1. Detailed scope of rehabilitation work resulting from joint inspection by Lender and mortgagor.
2. Lead-based paint reports and asbestos test reports for projects built before 1978.
3. Detailed Cost Estimate, Form HUD-92326.
4. Estimate Costs of Replacement Reserve items.
5. Form HUD-92264 must be completed in accordance with basic valuation instructions for Sections 221(d) and 220 processing Development of the "As Is" value and value for the land without improvements.
6. The HUD-92273 and HUD-92274 analysis used to support the income and expenses on the HUD-92264 must reflect the "as completed" property conditions.
7. Section 231 substantial rehabilitation cases requires two value estimates on the HUD-92264, a value subject to the completion of rehabilitation using all applicable approaches and an "As Is" value.

Section 223(f) for Refinance or Purchase of Existing Apartments

4B

I. PROJECT CONCEPT MEETINGS

It is strongly encouraged that all projects (both market rate and affordable) participate in a concept meeting with the program center, either in person or by teleconference, where the project has an early review before submitting a pre-application or direct to Firm application. The exhibits required for the concept meeting for Refinancing or Acquisition Proposals:

1. Section of the Act
2. Number of market rate and affordable units
3. Projected mortgage amount
4. Mortgage term and estimated remaining economic life
5. Refinance or acquisition
6. Basic information on developer and principals
7. Management company
8. Previous HUD experience
9. Geographic location with map
10. Photographs of the subject and immediate surroundings
11. Actual and effective property age / class
12. Physical condition (PCNA not required)
13. Prior / proposed renovations (per unit cost)
14. Discuss eligibility for Section 223(f) versus substantial rehabilitation
15. Amenities
16. Existing debt / cash out
17. Current occupancy (physical / economic)
18. Income and expenses
19. Discuss green / sustainability issues as appropriate
20. Discuss general market conditions, competitive properties and comparables
21. Environmental issues
22. Actual / potential risks and mitigating factors
23. Any anticipated waiver requests

II. EXHIBITS REQUIRED FOR APPLICATION FOR FIRM COMMITMENT

No pre-application exhibits are required, but the Lender is advised to make preliminary inquiries to determine whether or not its reviewers will be acceptable to HUD. The firm application exhibits are:

1. Transmittal letter.
2. Narrative Summary and Underwriting Recommendation
3. Form HUD-92013 “Application for Multifamily Housing Project” with application fee.
4. Form HUD-92013 – Supplement with information on the Sponsor and Mortgagor entity.

5. Form HUD 92013-E, Supplemental Application and Processing Form (Housing for the Elderly/Disabled).
6. Appraisal
7. Market Study
8. Completed Form HUD-92264, Multifamily Summary Appraisal Report and Form HUD-92264A, Supplement to Project Analysis.
9. Active Partner Performance System Participate Certification – Electronic or Paper 2530 are acceptable. Also applies to Lessees.
10. Disclosure of any identity of interest between Sponsor and Lender.
11. Byrd Amendment (lobbying certification and disclosure). See 24 CFR Part 87.
12. List of principals of Sponsor, Mortgagor Entity and business concerns.
13. Current Résumé for the Sponsor, and each principal of the Sponsor.
14. Organizational documents creating Mortgagor Entity, if applicable.
15. Verification of Social Security Number or Employer Identification Number.
16. Property Capital Needs Assessment: Physical Inspection Report, detailed list and cost estimates for critical and non-critical repairs and improvements, and estimate for Replacement Reserve Deposits.
17. A report from appropriate officials, such as Fire Marshal or Building Inspector, identifying any code violation(s) of record.
18. Lenders Review of PCNA Report.
19. Plans and specifications for repairs and improvements, if required.
20. Copy of Certificate of Occupancy or Final Inspection Report.
21. Property Insurance Schedule, Form HUD-92329.
22. Complete appraisal with supporting documents:
    a. Rental Housing Income Analysis and Appraisal, Form HUD-92264,
    b. Estimates of Market Rent By Comparison Form HUD-92273, and
    c. Operating Expenses Analysis Worksheet Form HUD-92274.
23. Evidence of site control (deed, purchase agreement, option).
24. Evidence of last arms-length transaction price.
25. Description of condition of property, list of repairs and improvements made in last two years and their estimated cost.
26. Current certified rent roll.
27. Occupancy history, by quarter for last three years.
28. A current Phase I Environmental Site Assessment.
29. If part of the project is devoted to commercial space, copy of lease or leases. Show of total square feet and amount, and percentage of total income used for commercial.
30. Evidence of permissive zoning.

31. Area map showing location.
32. Photographs of building.
33. Legal description of property and title report.
34. CPA or IPA certified balance sheets and operating statements.
35. As-Built" Survey and Form HUD-2457, Surveyor's Report.
36. Environmental report (to include lead-based paint and asbestos if project built in 1978 or earlier).
37. If private water supply or private sewage system is in use, report from City/County Health Officer stating that health standards are met.
38. List and conditions for supplemental grants or loans, if any. Grant and/or commitment letter if applicable.
39. If LIHTC, Historic or New Market tax credits are part of financing, provide copy of certification(s).
40. Certification approving release of banking and credit information.
41. Financial statements:
    a. Personal Financial and Credit Statement, Form HUD-92417.
    b. Financial Statements for Business Entities last 3 years, Schedule of Real Estate Owned; Schedule of Mortgage Debt and credit reports.
42. Certified statement by mortgagor listing all outstanding obligations on project.
43. Report on experience of management agent.
44. Management Entity Profile (Form HUD-9832).
45. Management Certification (Form HUD-9839A, B, or C).
46. Management Plan and Sample Lease.
47. Management Agreement, if applicable.
48. Form HUD 92013-E, Supplemental Application and Processing Form (Housing for the Elderly/Disabled).
49. Disc or removable drive of the underwriting file, exhibits and third party reports.

Sample MAP Invitation Letter Format

4C

Mr./Ms.

_____

_____

_____

Dear Mr./Ms.:

Subject: MAP Invitation Letter
No.
Section
(Name of Project)
(City/State)

This is to inform you that our staff has reviewed the pre-application materials for the subject proposal and finds it to be worthy of further consideration should you decide to submit a Firm Commitment application for mortgage insurance. There is a market for the proposal based upon our review of the appraisal and market study subject to updating all market assumptions before Firm Commitment. The site appears acceptable based on our preliminary inspection and the information provided.

In the event that you desire to continue with this project and submit an application for Firm Commitment, it is understood that the project will have the following characteristics:

Type of Unit	Sq. Ft.	Number	Monthly Market Rental
Efficiency	_____	_____	_____
One Bedroom	_____	_____	_____
Two Bedroom	_____	_____	_____
Three Bedroom	_____	_____	_____
Four Bedroom	_____	_____	_____
Total	_____	_____	_____

Equipment and Services included in the rent are:

Number of Parking Spaces: Enclosed _____ Open _____

Estimated Monthly Parking Rental $ _____

Residential Accessory Income $ _____

Commercial Area _____ sq. ft. Estimated Monthly Rental $ _____

The operating expense estimate of $_____ per unit per annum is preliminarily acceptable subject to updated and relevant data before the Firm Commitment. The total for all improvements appears to be within a reasonable range. Attached is the current wage decision for this area. Please contact the Labor Relations staff at _____ for any updates while preparing your Firm Commitment application.

Land value/as-is value will be determined at the Firm Commitment stage. Excess costs resulting from any unusual site conditions identified in the construction cost estimate at the Firm Commitment stage will be deducted from the land value fully improved (with offsite improvements installed). The HUD environmental assessment and HUD previous participation (Form HUD-2530) will not be completed until the Firm Commitment package is submitted to HUD.

It is important to understand that this letter is not to be construed as a commitment on the part of FHA to insure a mortgage for your proposal. It is intended only to establish general agreement on the basic concept, market, rents and expenses for your proposal. If the Firm Commitment application submitted is consistent with the pre-application submission, does not trigger the thresholds for a more extensive review, and no problems arise because of environmental or previous participation issues, HUD should be able to complete its review within the scheduled time. If there are significant changes from the concept agreed to at the pre-application submission, HUD will need more time to complete an extensive review and will not be bound by the scheduled review time and could result in rejection of the Firm Commitment application. Significant changes would include changes in:

a. Location,
b. Building type,
c. Project market that would cause HUD to reassess income expense and demand assumptions.
d. Rents, unit number, unit mix or gross project area that is great enough to affect market potential and/or require a new market study and HUD review.

Therefore, you are invited to submit a Firm Commitment application for mortgage insurance on Form HUD-92013, Application for Multifamily Housing Project, along with a fee of $3 (30 basis points) per thousand of the mortgage amount; or the balance of the 15 basis point market rate pre-application fee, with the required MAP Lender deliverables, by <*insert date 120 days after the date of the letter*>.

The Lender must advise HUD in writing within 30 days of the date of this letter of invitation whether or not it plans to submit an application for the particular project. If the Lender fails to notify HUD within the time required, the invitation letter expires, and the Lender will be required to repeat the pre-application process.

The application for a Firm Commitment must be submitted within 120 days of the date of the letter of invitation. The Hub or Program Center may authorize up to three 30-day extensions (or one 90-day extension) of this 120-day limit, but there is no requirement that the extensions be approved.

The Hub or Program Center will review the circumstances reported by the Lender to justify an extension of time. The Lender must certify and the Hub or Program Center must determine that the request to extend beyond 120-days is not likely to change the underwriting data on which the invitation was based or to undermine the feasibility of the project due to a change in the market or other factors determined at pre-application.

In a rare circumstance where there is a justifiable request for an extension of time beyond the approved 90-days, the Hub or Program Center Director may allow, the Hub or Program Center Director must request authorization to approve a further extension from the Director of the Office of Multifamily Development (Headquarters) or his/her designee. The authorization request must provide the additional time requested, the Hub or Program Center's recommendation, and the reasons the extension is needed. It may be sent and responded to by electronic mail.

Section 221(d)(3) applicants should be aware that HUD Headquarters requires prior approval of the firm commitment processing for all Section 221(d)(3) applications which are also subject to appropriations of credit subsidy.

Firm Commitment Special Conditions for Tax Credit and Master Lease Applications

4D

Guidance reflected herein requires that certain provisions be emphasized as Special Conditions in the Commitment for Insurance of Advances, Form HUD-92432. Add the following special conditions as they apply to applications for mortgage insurance:

A. Equity Contribution. Provide satisfactory evidence of an agreement that binds the Investor to timely and periodically pay to the mortgagor LIHTC Equity to contribute to the completion cost, in the aggregate amounts set forth in Form HUD-2880 and HUD-92013.

B. Equity Contribution. An equity contribution schedule acceptable to HUD must be provided prior to Initial Endorsement.

C. Equity Contribution. The Initial Equity Investment, amount is $_____ {twenty percent}. This amount must be reflected on the initial requisition (Form HUD-92448) and disbursed in its entirety at Initial Endorsement.

D. Equity Contribution. Subsequent equity contributions should be made at a time and in a manner during construction to ensure that the statutory limitations based on actual costs for the applicable FHA mortgage program are maintained during construction. To maintain the appropriate balance of tax credit equity and mortgage loan proceeds, at each infusion of tax credit equity, those funds may need to be utilized before the next disbursement of mortgage loan proceeds.

E. Cost Certification Exemption. Since the project is exempt from providing a cost certification, prior to Final Endorsement and when the project reaches substantial completion, an income and expense statement must be submitted covering the period from first occupancy (if occupancy occurred during construction) or from the date of substantial completion (as deemed by a HUD Inspector) through the period ending three months prior to the date of the first principal payment under the mortgage, as originally scheduled. The statement must be submitted at least 30-days before the date scheduled for Final Endorsement. If the income and expense statement evidences receipt of income (excess funds) during this period, the additional funds may be deposited into the reserve for replacement account, or used for approved non-mortgagable costs or improvements as determined by the allocating State Housing Finance Agency (HFA).

F. Deferred Drawings and Specifications. As an accommodation, this Commitment has been issued and based upon schematic drawings, instead of final drawings and specifications. At least 30-days before the scheduled date for initial endorsement, the Commissioner must receive the final drawings and specifications for review and approval to ensure consistency of design and cost. In the event that there is a net cumulative construction cost increase or change in the design concept, or a net cumulative construction cost decrease in the amount of more than two percent (2%), this Commitment shall be subject to and conditioned upon further approval of the HUD, to be evidenced in writing, and may be terminated and voided by the HUD, or additional conditions may be imposed, at HUD's option.

G. Master Lease. The policies and procedures involving master lease structuring to facilitate the use of tax credits are incorporated herein and made a part of this Commitment for insurance of advances, specifically including, without limitation, the terms and conditions contained in (a) Section 16.4, entitled "Programmatic Requirements," (b) Section 16.5, entitled "Firm Commitment Exhibits and Processing," and (c) Section 16.7 entitled "Actions Prior to Initial Endorsement, thereof. Without limiting anything contained in Chapter 16, all information submitted to HUD with the Application for Multifamily Housing Project, Form HUD-92013, to evidence the satisfaction of such terms and conditions shall be true and correct as of the date submitted, and must continue to be true and correct at the time of Initial Endorsement.

H. Master Lease. This commitment is subject to, and has been issued upon the reliance of, the successful (a) allocation to the project of LIHTC, Historic Tax Credits or New Market Tax Credits and (b) syndication of such credits, with an appropriate agreement for the timely infusion of equity there from, as shown on Forms HUD-2880 and HUD-92013, to assure completion of the project and pay other associated and incidental costs. In addition to the standard provisions that must be included in the organizational documents for the mortgagor entity, a provision must be added that prohibits any changes to the organizational documents that affect the obligations of the tax credit investor without the written consent of the Mortgagee and HUD.

H. Previous Participation. Notwithstanding the issuance of this commitment, this commitment remains subject to, and HUD's obligations hereunder are conditioned upon the satisfactory resolution, as determined by HUD, of the adverse items determined by HUD during the HUD Previous Participation review process.

Appendix 5

Architectural Analysis

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Common HUD Standards and Other Criteria for Sections 220, 221(d), and 231

5A

A. Minimum Property Standards.

1. Design must meet HUD Handbook 4910.1, Minimum Property Standards for Housing (MPS).

   a. Local Building codes or nationally recognized building codes accepted or designated by the local HUD Office are part of the MPS.

   b. The Field Office enforces and interprets accepted local building codes for HUD.

   c. The Field Office does not enforce local building codes for the local Government.

2. For community sewerage systems, use HUD Handbook 4940.3, Minimum Design Standards for Community Sewerage Systems.

B. Accessibility for Persons with Disabilities Requirements.

1. Uniform Federal Accessibility Requirements (UFAS) apply when compliance with Section 504/ or specific program criteria is required. There is a distinction between the application of the Fair Housing Act's design and construction requirements, which apply to "the design and construction of covered multifamily dwellings for first occupancy" after March 13, 1991, and Section 504/ the Uniform Federal Accessibility Standards (UFAS), which establish guidelines for accessibility by disabled persons in Federal and/or federally-funded facilities and may apply if HUD provides financial assistance to a project. The Americans with Disabilities Act may also be applicable, depending on the type of project insured.

2. Title VIII of the Civil Rights Act of 1968, as amended, commonly known as The Fair Housing Act (the Act) directs the Secretary of HUD to provide technical assistance to States, local governments, and other persons in implementing the accessibility requirements of the Act. Section 804(f)(3)(C) of the Fair Housing Act requires that all residential buildings which have four or more units and which are built for first occupancy after March 13, 1991 (referred to in the Act as "covered multifamily dwellings"), be designed and constructed to have at least one building entrance on an

accessible route, unless it is impracticable to do so because of terrain or unusual site characteristics. The accessibility requirements must be included in all of the dwelling units in buildings with elevators, and in all of the ground floor dwelling units in buildings without elevators. Moreover, accessibility in all common use and public use areas is mandated. They design and construction requirements for accessibility are:

a. Public and common use areas must be readily accessible to and usable by persons with disabilities;

b. All doors designed to allow passage into and within such dwellings are sufficiently wide to allow passage by persons in wheelchairs;

c. All premises contain the following:

(1) An accessible route into and through the dwelling unit;

(2) Light switches, electrical outlets, thermostats, and other environmental controls in accessible locations;

(3) Reinforcements in bathroom walls to allow later installation of grab bars; and

(4) Usable kitchens and bathrooms such that an individual in a wheelchair can maneuver about the space.

As a part of processing and commitment, the Lender's analyst will review construction documents for covered multifamily dwellings pursuant to the MPS (HUD Handbook 4910.1), and the Fair Housing Accessibility Guidelines (the Guidelines). The Guidelines provide minimum accessibility noncompliance. The Guidelines are found in the Federal Register, Vol. 56, No. 44, Wednesday, March 6, 1991. Additional material may be found in the Fair Housing Act Design Manual.

C. Commercial Facilities. The term "Commercial" is applied to any space or facility permitted and acceptable for "Nonresidential Use" from which income is derived or anticipated. However, facilities such as swimming pools and garages to be use solely by occupants are not considered commercial even though fees may be collected.

1. The nature and extent of nonresidential use are important for underwriting determinations. Basis of determinations are suitability, market demand, economic feasibility in the utilization of space, and Regulatory or Statutory limitations.

2. The aggregate commercial floor area may not exceed 10 percent of the gross building floor area and includes corridors, stairs, elevators, lobbies, and other service areas for commercial use, but excludes laundry space, project storage space, and interior resident parking.

3. Design of commercial facilities must be harmonious with the project and conform to standards of design and construction, and local zoning and building codes.

4. Do not include fixtures, equipment, furnishings or finish for commercial spaces in the mortgage unless customarily provided in competitive projects.

D. Day Care Facilities. Space for day care facilities must be adequate, appropriate to the market need, and conform to local and State requirements. In processing, it is considered as "Commercial" space except that the area of space for day care facilities may be provided over and above the maximum area allowed for commercial uses as stated in paragraph C above.

E. Carpet and Cushion. Wall-to-wall carpet and cushion may be included as part of the mortgage security. Carpet and cushion selected by the architect must comply with current applicable Use of Materials Bulletins.

1. Carpet is acceptable in all public spaces except laundry rooms, storage rooms, boiler rooms, and similar service areas.

2. Carpet is acceptable in living units except in kitchens and bathrooms.

F. Blinds and Draperies. Operable draperies, track and hardware, venetian blinds or shades are acceptable as part of the mortgage security when:

1. Appropriate to the property, considering types of windows, rental range, and occupants.

2. Primary uses are to control the intensity of natural light and to provide privacy.

3. The quality and type of materials, appearance, manufacture, manner of fastening and operations are suitable and sufficiently durable to avoid excessive replacement or maintenance expense.

G. Air Conditioning. Where air conditioning is required to provide year-round indoor comfort,

assure continued marketability, and prevent premature obsolescence, projects should be air-conditioned. In projects acceptable without air conditioning, assure air movement for summer comfort by adequate mechanical or cross ventilation. Particular attention should be given to the need for air conditioning in elevator structures, especially for senior citizens.

H. Eligible Equipment.

1. Equipment included as part of the mortgage security must be acknowledged by the mortgagor and Lender to be part of the real estate and:

   a. Be essential for successful operation and market acceptance.

   b. Have qualities in design, construction, materials and finishes which are not subject to early deterioration or obsolescence.

   c. Be appropriate to the location, the design of the building, and the anticipated occupants.

2. Equipment needed for operation and market acceptance, such as ranges and refrigerators, should be included. The equipment should be relatively long-lived.

   a. Replacement is paid for from a reserve for replacements account that is funded from project income.

   b. Many items formerly considered chattels by custom and legal precedent now have status as part of the real estate.

   c. Customs change and if doubts arise as to legal precedent concerning whether an item is chattel or real estate, essential and required items may be covered by a security agreement or chattel mortgage, as well as being covered by the mortgage on the real estate if deemed necessary by the Lender and its attorneys.

3. Equipment that may not be included:

   a. Supply items, utensils, tools, vehicles, portable equipment, furniture, furnishings, or accessories normally provided by residents or management

   b. Built-in or attached furniture.

I. Water and Sewerage. Public water and sewerage facilities are generally required for multifamily projects. If the extension of public facilities is infeasible, construct a water and/or sewerage system as part of the project or provide services from existing offsite privately owned systems with continuing service at reasonable rates.

1. Water and/or sewerage facilities must:

   a. Provide a sufficient supply of water with adequate pressure, and satisfactory bacterial and chemical qualities.

   b. Provide a sewerage system with adequate collection, treatment and final disposal of domestic waste, which requires minimum maintenance and will not endanger the public health.

2. Duplicate water and sewerage systems are not acceptable except where it is determined that the construction of a single system will be infeasible due to the topography of the site.

3. Individual septic systems or sewerage systems designed to dispose of effluent by subsurface soil absorption methods are generally not suited for multifamily construction because of maintenance problems. Satisfactory operation can be expected only under unusually favorable soil conditions. When these methods of sewerage disposal are proposed, an environmental (sanitary) engineer, with no other interest in the project, should be hired by the mortgagor to investigate soil and site conditions and make recommendations. A copy of the report must be available to the mortgagor's Architect and be included in the exhibits submitted for review by the Lender's analyst.

4. Privately Owned Offsite Water and Sewerage Systems.

   a. Evidences of acceptable control are:

      (1) Certificate of Convenience and Necessity from the State Utility Regulatory Commission.

      (2) Franchise from local unit of Government

      (3) Trust Deed

(4) Third Party Beneficiary Agreement

(5) An incorporated nonprofit owners association.

b. If control of continuity of service and the equitability of the service rate schedule is other than (1) above, all legal documents and other appropriate exhibits must be acceptable to HUD's Counsel.

5. All community systems and privately owned systems must meet local health authority or EPA MCL standards.

J. High Pressure Gas and Liquid Petroleum Transportation Pipelines.

1. All parts of a residential structure must be at least 10 feet from the outer boundary of the pipeline easement for pipeline maintenance access.

2. Surveyor Identification of Gas and Hazardous Liquids Pipelines Regulated by 49 CFR Parts 192 and 195, and A&E Collection of Pipeline Operator Compliance Certifications.

a. PURPOSE:

(1) Eliminate requirements for surveyors to identify gas and hazardous liquids pipelines regulated by the Department of Transportation under 49 CFR Parts 192, Transportation of Natural Gas and Other Gas by Pipeline: Minimum Federal Standards, and 49 CFR Part 195, Transportation of Hazardous Liquids by Pipeline, for such pipelines that are within 220 yards of the project site; and

(2) Eliminate requirements for HUD A&E to collect documentation regarding compliance of gas and hazardous liquids transportation pipelines regulated by the Department of Transportation under 49 CFR Parts 192 and 195.

Note: The surveyor must still identify all easements and pipelines that cross or are adjacent to the project, as otherwise prescribed by the Minimum Standard Detail Requirements and Classifications for ALTA/ACSM Land Title Surveys dated 2005, and Form HUD-92457, Surveyor Instructions and Report.

b. HUD REQUIREMENTS:

(1) This cancels HUD requirements calling for identification on the survey of high pressure gas and liquid petroleum pipelines within 220 yards of the property; and regarding collection of pipeline operator certifications for compliance with 49 CFR Parts 192 and 195;

(2) Modifies the surveyor's certificate to read as follows:

"I made an on the ground survey per record description of the land shown herein located in (*insert city or town, county, township. etc.*), on (*insert date*); and that it and this (these) map(s) was (were) made in accordance with the HUD Survey Instructions and Certificate, Form HUD-92457, and meet the requirements for a Land Title Survey, as defined in the 'Minimum Standard Detail Requirements for ALTA/ACSM Land Title Survey,' dated 2005."

"To the best of my knowledge, belief and information, except as shown herein: There are no encroachments either way across property lines; title lines and lines of actual possession are the same; and the premises are free of any (subject to a) 100/500 year return frequency flood hazard, and such flood free (flood) condition is shown on the Federal Flood Insurance Rate Map, Community Panel No. _____(state, if none)."

K. Reports. The Lender's analyst must assure that the environmental and/or valuation required reports and requirements, such as seismic, flooding (Executive Order 11988), underground storage tanks, etc., contained in the application are properly evaluated and are adhered to in the project design.

L. Subsurface Exploration. Before foundation design and application for Firm commitment, reliable information about subsurface conditions and foundation recommendations must be made available to the Lender's analyst by the mortgagor.

1. The Architect must advise the owner of the scope and type of soils information and/or subsurface investigation required for structural design.

2. The mortgagor must provide the services of a registered design professional for determining subsurface conditions. These services shall be provided in accordance with the Owner-Architect Agreement.

3. The Lender's architectural analyst will assure that the architect has comprehensive, well documented soils information and that project foundation design follows the report

recommendations. When necessary, the Lender's architectural analyst may request engineering help in reviewing soil reports and related designs.

4. Soils investigation shall be in accordance with Chapter 18 of the International Building Code, except that an investigation and report is required for every project involving new construction, whether or not required by the building official.

M. Noise Abatement and Control. The Lender's architectural analyst in collaboration with the mortgagor's Architect and the Lender's appraiser must identify existing and potential sources of noise which represent a threat to the serenity and quality of life in, and the economic soundness of, HUD-insured multifamily housing projects.

1. The mortgagor's Architect will recommend to the Lender's architectural analyst and to HUD, the appropriate means of separating uncontrollable noise sources from residential areas.

2. External and interior noise exposure standards should be complied with.

N. Other Tests. Other exploration or tests may be required for environmentally hazardous materials such as asbestos, radon, PCB, gasoline, methane, etc, if:

1. History indicates possible problems in project area.

2. Previous usage of the site indicates possible contamination.

3. There is evidence of possible contamination or presence of hazardous material.

O. Energy Efficiency. The project design must achieve HUD energy efficiency standards for new construction, which shall meet or exceed the requirements of the 2006 International Energy Conservation Code (IECC), or in the case of multifamily high rises (defined as residential structures of 4 or more stories), the requirements of the American Society of Heating, Refrigerating, and Air-Conditioning Engineers (ASHRAE) Standard 90.1 - 1989 (or later versions as adopted by the Secretary of HUD), and shall be cost-effective with respect to construction and operating costs on a life-cycle cost basis. The Department, in cooperation with the Environmental Protection Agency and the Department of Energy, has adopted a wide ranging energy action plan for improving energy efficiency in all housing programs, which includes encouraging program participants to use Energy Star products.

For guidance on the life-cycle cost analysis, see 1999 ASHRAE Application Handbook, 35.8,

and NIST "Building Life-Cycle Cost" Program, Version 4.3 User's Guide and Reference Manual.

Additional HUD Standards and Other Criteria for Sections 220, 221(d), and 231 - Substantial Rehabilitation

5B

STANDARDS. Substantial rehabilitation must comply with common HUD standards in Appendix 5A, except as modified herein and applicable local codes, ordinances, and guidelines.

A. All new construction or additions that enlarge existing buildings are not rehabilitation and must meet applicable codes and standards for new construction.

B. Rehabilitation projects are subject to environmental requirements in:

1. Title 24 of the Code of Federal Regulations (CFR), Parts 50 and 55, and

2. The statutes, Executive Orders, and HUD Standards and criteria (24 CFR Part 51) cited in 24 CFR Part 50.4. Compliance shall be documented on Form HUD 4128.

C. Historic Structures and/or Districts: Projects that include historic structures or affect historic structures or districts are subject to 24 CFR Part 50.4 and must comply with:

1. Section 106 of the National Historic Preservation Act and

2. Secretary of the Interior, Standards for Rehabilitating Historic Buildings.

D. A full Environmental Assessment, Form HUD-4128, is required for the following activities which are not categorically excluded pursuant to 24 CFR 50.20 and involve or include:

1. Additions (new construction);

2. Rehabilitation with estimated costs that are more than 75 percent of the total estimated cost of replacement after rehabilitation;

3. Conversion of non-residential use (hotels, offices, stores, lofts, etc.) to residential occupancy; or

4. Change of unit density by more than 20 percent.

E. Seismic Resistance. See Appendix 5D, paragraph A.

F. Fire Protection. See Appendix 5D, paragraph B.

G. Accessibility for Persons with Disabilities. Only if required by program under Section 504 or the ADA or by the Fair Housing Act, in which case noncompliant design and construction must be retrofitted. See Appendix 5A, paragraph B.

H. Lead-Based Paint Hazard Elimination.

Refer to Part 35 of Title 24 of the code of Federal Regulations (24 CFR Part 35)

I. Asbestos Hazard Elimination.

Refer to Environmental Protection Agency regulations in Title 40, Part 61 of the Code of Federal Regulations (40 CFR Part 61).

J. Energy Savings.

HUD has published an informational booklet entitled "HUD Rehabilitation Energy Guidelines for multifamily Dwellings."

Additional HUD Standards and Other Criteria for Projects Insured Pursuant to Section 223(f)

5C

In general, all the instructions in Appendix 5A for Sections 220 and 221(d) of the National Housing Act apply to projects insured pursuant to Section 223(f), except as modified herein.

STANDARDS. Eligible properties are existing construction. The criteria for acceptance are not the same as for proposed construction. The property in its present condition, must meet the general criterion for livability without the necessity of substantial rehabilitation in order to be eligible for consideration under the Section 223(f) program. The objective is to assure an acceptable risk through only repair requirements. The Minimum Property Standards (MPS) apply in the following manner:

A. The General Acceptability Criteria shall be met with the requirement for an accessible primary entrance for the physically handicapped.

B. The property shall comply with the general intent of all other chapters of the MPS.

C. Compliance with Statutory and Regulatory Requirements is mandatory. These include:

1. Lead-based paint hazard elimination. See 24 CFR Part 35

2. Asbestos hazard elimination. See 40 CFR Part 61.

3. Flood hazard limitations.

4. Smoke detector(s):
   a. Smoke detector(s) must be installed:
      - In all bedrooms;
      - Outside each sleeping area in the immediate vicinity of the bedrooms;
      - On all levels of the dwelling unit, including basements.
   b. Installation of required smoke detectors is a Critical Repair.
   c. Battery powered smoke detectors are permitted. See Appendix 5D, paragraph B for requirements.

D. Seismic Resistance. See Appendix 5D, Paragraph A.

E. Accessibility for Persons with Disabilities. Only if required by program under Section 504 or the ADA or by the Fair Housing Act, in which case noncompliant design and construction must be retrofitted. See Appendix 5A, paragraph B."

1. Regulation and/or Program requirements. If an existing property was built before the enactment of accessibility requirements, there is no requirement for upgrading the property to current accessibility requirements, with the following exceptions:
   a. The property has a feature that triggers a regulation requiring an upgrade to current accessibility requirements;
   b. The program requires an accessibility upgrade for any individual room or space, whenever the room or space is substantially altered. This would apply even when the overall scope of repair work for the entire project does not qualify as substantial rehabilitation.
2. Meeting Fair Housing Act Requirements.
   a. If a project built for first occupancy after March 13, 1991 is submitted for 223(f) refinancing and the PCNA (See Appendix 5G) inspection reveals that it does not meet all of the design and construction requirements of the Fair Housing Act, the Department requires the owner to modify/retrofit the project to meet these requirements as a condition of mortgage insurance. In no case may the Department insure such a project without a modification/retrofit plan. The extent and cost of the modifications/retrofits will determine whether the project is feasible as a 223(f) or whether to resubmit it as substantial rehabilitation. See Appendix 5A, Paragraph B.2 for an outline of Fair Housing Act requirements.
   b. The modifications/retrofits may commence after Initial/Final Closing, but must be completed no later than one year after the Initial/Final Closing date (See Chapter 5 Section 5.24.A).
      (1) Correction of Fair Housing Act noncompliance may be either critical or non-critical repairs. It is the responsibility of the Needs Assessor to determine the status of each and every correction.
      (2) Any Fair Housing Act correction that poses a direct threat to life and safety (example: the apartment entry door is too narrow for wheelchair passage) must be treated as a critical repair and corrected before closing, along with all other critical repairs. However, any Fair Housing Act correction that is not a direct threat to life and safety (example: a turning radius in the bathroom that is a fraction too small for a single turn to get to the bathtub, requiring the wheelchair user to use extra motions to maneuver the wheelchair into position) may be treated as a non-critical repair, which can be corrected up to one year after Initial/Final Closing.
   c. Except in extraordinary circumstances, modifications/retrofits of the public and common areas of the project must commence within thirty days of the Initial/Final Closing date.
   d. Individual units.
      (1) Modifications/retrofits for individual units in the project must be scheduled to commence within sixty days after the Initial/Final Closing date.

(2) Advance notice to residents. Immediately after the issuance of the Firm Commitment, residents must receive written notification indicating the modifications/retrofits to be performed, the anticipated start date and work schedule, and, if necessary, the schedule of temporary relocation for each unit.

e. In all cases, once these structural modifications/retrofits are begun, the work should be completed without unreasonable delay. All structural modifications/retrofits must be completed within one year after the Initial/Final Closing date.

f. All such modifications/retrofits must conform to the escrow and inspection requirements contained in Chapter 12.

F. Survey Requirements:

1. An "as built" survey, signed by a registered surveyor, showing all improvements on the site, on or before the date of the application submission. The survey submitted with the application may be a copy of one several years old. However, a current "as built" survey, showing all improvements on the site after all repairs are complete, will be required. If deferral of non-critical repairs is approved, the "as built" survey must be submitted after all such repairs are completed, and the submission of the survey will be a condition for the release of the remainder of withheld repair escrow funds. The survey must include:

   a. If the proposed repairs include site grading, provide existing contours at one-or two-foot intervals, except that for steeply sloping sites, the intervals may be five feet. If the repairs do not involve site grading, contours are not required.

   b. City, county, state, and lot and block numbers of the property and adjacent sites.

   c. Distance to the nearest street, dimensioned length of each boundary, such as monuments, markers, fences, etc., and all encroachments or deviations from description of the subject property or conflicts with descriptions of adjacent properties.

   d. Easements, rights-of-way, setback lines, and other restrictions.

   e. Existing streets, alleys, and drives, street names, and other pertinent data. Include any surfacing and curbs that are being repaired.

   f. If the proposed repairs include utility lines, provide location and sizes of all such lines included in the repairs. If repairs include sewer lines, provide invert sewer elevations and direction of flow. If repairs do not include utilities, this information is not required.

   g. If the proposed repairs include arbor work on tress that can be preserved, provide location of all such trees undergoing preservation.

   h. Location and description of all existing structures.

   i. Legal description of the property, with total square footage and acreage.

2. Certification language. Form HUD-92457M, HUD Survey Instructions and Report, has mandatory certification language that the surveyor must put on the survey map/plat. The American Land Title Association/American Congress on Surveying and Mapping

(ALTA/ACSM) has its own mandatory certification language that differs from HUD's language. The American Land Title Association/American Congress on Surveying and Mapping (ALTA/ACSM) has its own mandatory certification language that differs in wording from HUD's mandatory certification language on Form HUD-92457M. HUD will permit the required ALTA/ACSM certification to appear on the survey map/plat along with the required HUD certification.

Seismic Resistance and Fire Protection Standards for Substantial Rehabilitation and Projects Pursuant to Section 223(f)

5D

Projects must comply with the provisions of each referenced standard, and the following:

A. Seismic Resistance for Substantial Rehabilitation and Existing Projects pursuant to Section 223(f). Structures in seismic zones 3 and 4 must meet three fourths (3/4) of the seismic force level resistance contained in FEMA-310, Handbook for the Seismic Evaluation of Buildings – A Pre-standard, FEMA-356, Pre-standard and Commentary for the Seismic Rehabilitation of Buildings, and FEMA-274, NEHRP Commentary on the Guidelines for Seismic Rehabilitation of Buildings.

   1. A seismic hazard analysis of the building(s) must be made by a registered engineer familiar with lateral force design, where applicable code requirements at the time of construction did not equal or exceed the referenced seismic standards.

   2. The evaluation must include an examination of the structure for continuity, ductility, and resistance to lateral forces.

   3. Structural elements and connections between elements must be strengthened and new elements installed as required, if the existing structure does not provide three fourths (3/4) of the seismic force level resistance required by paragraph A above.

B. Fire Protection.

   1. Fire/smoke detection, alarm and communication systems must comply with the Life Safety Code, NFPA 101, for the entire project.

      a. The 2006 NFPA 101, paragraph 31.3.4.5.1, states that "…approved single station smoke alarms shall be installed … outside every sleeping area in the immediate vicinity of the bedrooms and on all levels of the dwelling unit, including basements", and the regulation in 24 CFR 200.76 requires that smoke detectors must also be installed inside each sleeping area.

         Accordingly, smoke detectors must be installed:

         - Inside all bedrooms
         - Outside every sleeping area in the immediate vicinity of the bedrooms, and
         - On all levels of the dwelling unit, including basements.

      b. For Section 223(f) projects, installation of required smoke detectors is a Critical Repair.

      c. The regulation does not specify whether the required smoke detectors must be hard wired or battery powered. However, Section 3.3.9.1 of NFPA 101 permits a battery-operated device.

         (1) For substantial rehabilitation projects, regardless of the scope of work, hard wired smoke detectors are required.

(2) Considering the difficulty, time and expense of feeding electrical wiring through the walls of existing buildings, battery-operated smoke detectors are acceptable in Section 223(f) projects, under the following condition:

- The smoke detectors must be powered by power cells having the following characteristics:
  - The cells must have a ten-year life.
  - The cells must be tamper-resistant;
  - The cells cannot be used in any other toy or appliance;
  - The smoke detector may have a manual (but not automatic) silencing device to clear unwanted alarms such as cooking smoke.

Smoke detectors as described above appear to meet the intent of the smoke alarm requirements in Section 9.6.2.10 of NFPA 101.

2. Any new construction must have a sprinkler system as required by NFPA 101.
3. Substantial rehabilitation of the fully repaired structure (or floors/wing(s) to which work is limited) must comply with NFPA 101 fire protection provisions for new construction.
4. New additions must be separated from existing structures, even if the entire facility is included under one mortgage. Separation must equal or exceed:
   a. Two-hour rated firewall;
   b. One and one half (1 ½) hour protected openings;
   c. Class B labeled fire doors;
5. New work on substantial rehabilitation projects must comply with standards for new construction.

Firm Commitment Drawings and Specifications to be Submitted by the Mortgagor's Architect

5E

A. Cover sheet:

1. Project name and identification number.

2. Spaces for signatures of design Architect, Architect administering contract, owner, contractor, Lender, and bonding company.

3. Tabulation of living units:

   a. Number of units for each type.

   b. Number of units and type in each building.

   c. Non-rental living unit.

   d. Number of parking spaces, open and covered.

B. Index of drawings by name, numbered consecutively, with date of preparation and latest revision date. Consecutive numbering is required for each drawing category (Architectural, Land Improvements, Structural, Plumbing, HVAC, Electrical, etc., shown as A-1, A-2, A-3… L-1, L-2, L-3, etc.), but absolute consecutive numbering of the entire set is optional, and would appear only in addition to the categorical numbering.

C. Topographic survey, that is, a "transit survey" at a minimum scale 1" = 40'-0", recent, dated, and signed by a registered surveyor, and including:

1. Contours at one-or two foot intervals, except that for steeply sloping sites, the intervals may be five feet.

2. City, county, state, and lot and block numbers of the property and adjacent sites.

3. Distance to the nearest street, dimensioned length of each boundary, such as monuments, markers, fences, etc., and all encroachments or deviations from description of the subject

property or conflicts with descriptions of adjacent properties.

4. Easements, rights-of-way, setback lines, and other restrictions.

5. Existing streets, alleys, and drives as well as surfacing, curbs, street names, and other data.

6. Location and sizes of public utilities with invert sewer elevations and direction of flow.

7. Preservable trees.

8. Location and description of all existing structures.

9. Legal description of the property, with total square footage and acreage.

D. Plot plan at a scale not less than 1”= 40’- 0” showing:

1. Land boundaries, dimensions, and North Point.

2. Streets, alleys, or roads adjacent or within the property boundaries, together with walks, curbs, pavements, steps, ramps, play areas, parking areas, and drying yards, and utilities such as gas, water, electric, and sewer lines.

   a. Dimension or size with distance from location points, material indication for such items as walks and pavements, and extent of each.

   b. Indications of “new” or “existing” and public dedication of any streets or alleys in the project.

3. Buildings, building designations, location dimensions, and overall dimensions.

4. Elevations of first floor, elevations of finish and existing grade at building corners and entrances, elevations of curbs and streets, and invert elevations of main sewer and direction of flow.

5. Utilities servicing the property, or distance to point of connection and utility lead-ins of service connections; yard lighting; lawn hydrants and lawn sprinkler systems with the pipe sizes and controls; drains; and fire hydrants.

6. Retaining and garden walls, fences, guard rails, garages and accessory structures, with dimensions.

7. Existing trees and other natural features and whether to be removed or preserved.

E. Grading and drainage plan at a scale not less than 1”= 40’- 0” when essential information cannot be clearly shown entirely on the plot plan.

1. Grade elevations at all building corners and at entrances, walks, drives, parking areas, terraces, yards, walls and steps, and first floor elevations. Existing and proposed grading contours at appropriate intervals.

   a. Yard and roof drainage with controlling grades and dimensions of drainage lines, culverts, catch basins, drainage inlets, gutters, curbs, drainage disposals, and any existing facilities.

F. Planting plan at a scale not less than 1”= 20’- 0” indicating:

1. Outline of buildings and other improvements with physical features of the site to establish the location and relationship of planting and landscape construction.

2. Distribution of plant material, location, quantity and key number of each general species in each group; outline of planting beds, primary lawn areas, secondary lawn areas and existing trees to be preserved or transplanted.

3. List of plant material using English and Latin names, key number for each variety for reference to plan, and the size, quality or other description.

G. Basement plans for each building type at a scale not less than 1/8”= 1’- 0.” (Foundation plans when no basements.)

1. Dimensions and names indicating use of spaces, with the layout of permanent equipment.

2. Location of structural elements with dimensions or notes as to: thickness and size; windows; vents; areaways; doors; lights and switches; drains; sumps; etc. Unless there is a separate foundation plan, show locations and size of footings, piling and other substructure work.

3. Large-scale drawings or details of spaces not clearly shown.

H. Floor plans:

1. Unit floor plans at a scale not less than ¼”= 1’- 0” for each basic type living unit and any major variation. Separate unit plans are not required when the general floor plans are provided at ¼-inch scale and contain all essential information.

   a. Partitions to scale; rooms, closets and hall dimensions; over-all dimensions; window locations and type designations referring to schedule showing design, thickness, and size; dimensioned stair locations, runs and width, landings and handrails.

   b. Plumbing fixtures; soil and vent stacks; kitchen cabinets and equipment; electric lights; switches, receptacles, and special power outlets; closet shelving and clothes rods; radiators or other heating devices, chimneys, and all other such items.

   c. Location of structural elements such as columns, lintels, joists, beams, girders, and bearing partitions. Show sizes, spacing and direction of members. Separate structural drawings are required where the structural information would obscure other information.

   d. All conditions where units are to join other units; end-unit conditions.

   e. Identification of living unit types by a number or letter.

2. General floor plans at a scale not less than 1/8” = 1’- 0.”

   a. Dimensional relation of living and building units with over-all dimensions of building units and buildings, partition arrangement and fenestration of end units, units at corners and units at offsets; other partitions as necessary to show variations from the typical unit plans and relation of rooms in adjacent living units, wall separating building units, and their material and thickness.

   b. Buildings and those units identified by numbers or letters.

I. Roof plans at a scale not less than 1/8” = 1’- 0.”

1. Relation of intersection of the various building unit roofs; direction of slopes; parapets, chimneys, vents, and other projections; downspout locations and sizes.

2. Omit where the essential information can be shown clearly on the plot plan or other drawings.

J. Elevations:

1. General elevations at a scale not less than 1/8" = 1'- 0." Exterior design of all sides of buildings with existing and proposed grades at buildings, floor lines and elevations, floor height dimensions, roofs, attic vents, parapets, cornices, downspouts, openings, material notes, and other essential features.

2. Typical elevations at a scale not less than ¼" = 1'- 0" to show portions of facade with a special exterior design. Show materials, jointing, special features, windows, doorways, cornices, parapets, and details.

K. Sections:

1. Outline sections - scale not less than ¼"=1'- 0". Show various height conditions, cross sectional characteristics, and floor level relations, when other drawing information is not adequate.

2. Detail sections - scale not less than 3/8"=1'- 0". Show each type of exterior wall and bearing wall or partition, from footings to roof.

3. Exterior wall sections - scale not less than 3/8"=1'- 0". Show complete construction of walls with thickness at various stories, floors, furring, waterproofing, ceilings, roofs, including pitch and flashings, room heights, anchorage and bearings, cornice and gutter, insulation, vapor barrier, foundation walls and footings, conditions at various basement depths, basement floors or access space, roof space, attic and foundation vents.

L. Details at a scale not less than 3/8"=1'- 0". Provide the following except where such features do not occur:

1. Front and rear entrances, plan of each with elevations and sections.

2. Stair plans and sections showing stringers, treads, risers, newels, balusters, handrails, rise, run, and headroom.

3. Kitchen cabinet plans, elevations and sections.

4. Bathroom plans with elevations showing accessories and cabinets.

5. Entrance lobbies.

6. Platforms and areaways.

7. Special exterior and interior details, such as bay windows, dormers, cupolas, vents, fireplaces, and built-in furniture.

M. Schedules:

1. Door schedules - size, thickness, material and design of each door, with plan identification. Fire doors, show rating.

2. Window schedule - size, thickness, materials and design of each window, with plan identification.

3. Finish schedule - material and type finish of floors, base or wainscot (with height), walls, ceilings and trim for various rooms or spaces.

N. Structural: Drawings and details as appropriate, with complete structural information, must be provided when such information cannot be shown on general drawings without obscuring other information.

O. Mechanical: Heating, cooling, plumbing and electrical layouts on separate drawings unless the systems are simple enough to be shown on other drawings. Include all pertinent design data. Show special mechanical installations separately.

1. Heating drawings for each system (information in specification should not be on drawings).

   a. Location and size of boilers, furnaces, or heaters; the make, model number or type and net output of each.

   b. Layout, location, and sizes of supply and return piping, ducts, risers, and branches,

and insulation locations.

c. Location, sizes and output in BTU of radiators, registers, grille and panel surfaces, valves, vents, traps, dampers and other accessories; make, model number or type of each.

d. Make, model number, and firing rate of all firing equipment, and similar detailed data on other components of each system, such as, controls, pumps, blowers, and filters.

e. Location, type, manufacturer's name, and model number of domestic water heating and related equipment including: storage, arrangement and sizes of connecting piping; make and model number and other pertinent information for control equipment and safety devices.

f. Design data for the system, including outside design temperature, boiler operating temperature, BTU output, pressure or temperature drops, air temperatures at registers, pump or fan capacities, volumes, and velocities, heat loss of each building and total calculated heat load connected to each heating system; net output in BTU of each boiler and system.

g. Design data for each domestic hot water system and, when connected to a heating system, the additional heat load included in the total for the connected system.

2. Plumbing drawings:

a. Horizontal sewer and drain systems with soil, waste, and vent stacks; branch wastes and vents; drains, cleanouts, traps, sump pumps, etc., connections to sewer, sizes of lines and stacks. Diagram of typical stack including soil, waste, and vents.

b. Cold water distribution system, size of mains and branches, location of hose bibs, valves and drains.

c. Hot water distribution system together with circulating lines and pumps, valves, sizes of mains and branches.

d. Gas distribution system, size of mains and branches, meters, etc.

3. Electrical drawings:

a. Service lines, primary distribution and secondary distribution, service characteristics and wire sizes.

b. Meter and panel locations and manner of mounting.

c. Interior distribution and wiring of typical units.

d. Lights, receptacles, switches, special purpose outlets, and connections to equipment if not on the architectural plans.

e. Yard and grounds lighting and lighting of all public and common spaces and controls.

f. Power riser diagram and switchboard schedule.

g. Fire detection and alarm system riser diagram and schedule.

h. Symbol list.

4. Air conditioning drawings:

a. Locations, cooling capacity, and horsepower of compressor; cooling tower condensing units; and individual cooling units. Make, model number, and rating.

b. Layout of system including ducts, grilles, registers, diffusers, pipe sizes, and location of valves, vents, dampers and controls.

c. BTU load for each space, size and rating of equipment.

d. Design data for the system, including: CFM space requirements; blower ratings, type condenser cooling; inlet and outlet water temperature; and GPM water-flow rate.

e. Electric wiring layout, location of motors, fans, pumps, switches, and their load requirements.

P. Any other drawings required by lender.

Q. Appropriate general and supplementary conditions and Davis-Bacon wage rates (where applicable).

R. Contract specifications: Use a currently supported version of CSI Master Format specifications of the Construction Specifications Institute (CSI).

1. Describe all materials, equipment, and construction and include two, and preferably three, comparable products where practicable, or specify by performance characteristics.

2. Include the latest edition of the "General Conditions of the Contract for Construction", AIA Document A201.

3. Fully describe all materials, including alternates, and do not use general references to HUD's Minimum Property Standards. Do not include the words "or equal".

4. Divide into sections separately describing the work to be done by each trade essential to project completion. Consecutive page numbering is required for each trade category (Concrete, Masonry, Metals, etc.), but absolute consecutive numbering of the entire specification is optional, and would appear only in addition to the trade numbering. Include the following items:

   a. A cover sheet: Must include Title of project, the lender project number, project location, and a signature block setting forth:

      IDENTIFICATION

      Architect (Print Name) by (Signature)
      Owner (Print Name) by (Signature and Title)
      Contractor (Print Name) by (Signature and Title)
      Lender (Print Name) by (Signature and Title)
      Bonding Co.(Print Name) by (Signature and Title)
      Date_____

   b. Index.
      (1) Divisions with name.
         (a) Trade, name and page number.
         (b) Trade section, name and page number.

(2) Pages numbered consecutively

c. Conditions.

(1) General Conditions of the Contract for Construction, AIA Document A201, latest edition.

(2) Supplementary Conditions of the Construction Contract, Form HUD-2554, latest edition.

(3) Architect's Supplementary Conditions, if any.

d. Trade sections. Include:

(1) Complete description of all work to be performed. This will include scope of work, materials and workmanship.

(2) Necessary specific instructions for coordinating the work with other trades.

e. Methods of Specifying.

(1) Performance. List required qualities of products and assemblies and end result.

(2) Reference Standards. Incorporate references to nationally recognized standards published by industry associations, testing organizations and government, such as American National Standards Institute (ANSI), Underwriters' Laboratories (UL), and Department of Commerce (DOC).

(3) Proprietary. List products and assemblies by manufacturer or brand name, and grade or model.

(a) Include at least two comparables.

(b) Use a single brand only if there is no comparable.

f. Unacceptable.

(1) Use of the words "or equal".

(2) Reference to HUD or HUD publications, such as:

(a) Minimum Property Standards (MPS),

(b) Materials Bulleting (UM),

(c) Materials Releases (MR), and

(d) Structural Engineering Bulleting (SEB).

(3) Cash or lump sum allowances.

S. Offsite Drawings and Specifications.

1. Offsite improvements are those required to service the project but outside of the property boundary lines.

a. Include utilities, walks, curbs, gutters, streets, drainage structures, landscaping, and similar improvements beyond the property lines.

b. Do not include short extensions of utilities, walks, drives, drainage structures and similar improvements beyond the property lines which connect with those next to the property lines.

2. Offsite improvements may be included in the contract drawings and specifications but the extent must be clearly defined on the plot plan and in the specifications.
3. Complete, separate offsite drawings and specifications are preferred.

T. Utility Analysis. If required by the Hub Director, the mortgagor's Architect will prepare a utility analysis. For HUD energy efficiency standards see Appendix 5A, Paragraph O. For guidance on the life-cycle cost analysis, see 1999 ASHRAE Applications Handbook, 35.8, and NIST "Building Life-Cycle Cost" Program, Version 4.3 User's Guide and Reference Manual.

HUD Architectural Review Report for Pre-Application Exhibits

5F

HUD Office Name _____

Pre-Application Submission Date _____

Project Name _____

Project Location (City, State) _____ , _____

MAP Lender Name _____

Summary of HUD Architectural Review

A. Architectural/Engineering exhibits (including Mortgagor's Architect's Basic Work Write-up for Substantial Rehabilitation projects)

If incomplete, specify:

B. Conformance to HUD Standards

If unacceptable, indicate reasons:

C. Site conditions:

1. New construction projects:
   a. Placement of residential building(s)
   b. Unusual site conditions

If unacceptable, indicate reasons:

2. Substantial rehabilitation projects:
   a. Mortgagor's Architect's Basic Work Write-up

If unacceptable, indicate reasons:

D. Residential building(s):

1. Lobby floor:
   a. Circulation
   b. Mortgagor's Architect's Basic Work Write-up (for substantial rehabilitation projects)

If unacceptable, indicate reasons:

2. Typical floor:
   a. Circulation

b. Mortgagor's Architect's Basic Work Write-up (for substantial rehabilitation projects)
c. Acceptability of design

If unacceptable, indicate reasons:

3. Typical apartment layout(s):
   a. Circulation
   b. Mortgagor's Architect's Basic Work Write-up (for substantial rehabilitation projects)
   c. Size and marketability (determined by appraiser)
   d. Acceptability of design

If unacceptable, indicate reasons:

4. Structural system (Include Mortgagor's Architect's Basic Work Write-up for substantial rehabilitation projects)

If unacceptable, indicate reasons:

5. Exterior finish (Include Mortgagor's Architect's Basic Work Write-up for exterior doors, windows and building finish for substantial rehabilitation projects)

If unacceptable, indicate reasons:

6. Rehabilitation of roof(s) (substantial rehabilitation projects)
   a. Mortgagor's Architect's Basic Work Write-up

If unacceptable, indicate reasons:

I have reviewed the subject project and hereby make the following recommendation(s):

Reviewer:

Name of Reviewer _____

Signature and Date of Review _____ Date _____

Concurrence:

Name of Team Leader _____

Signature and Date of Concurrence _____ Date _____

HUD Architectural Review of Lender's Architectural Analyst's Report for Firm Exhibits - New Construction & Substantial Rehabilitation

5F.1

HUD Office Name _____

Firm Commitment Submission Date _____

Project Name _____

Project Location (City, State) _____ , _____

MAP Lender Name _____

Summary of HUD Architectural Review

A. Firm Commitment deliverables:

If incomplete, specify:

B. Lender's Architectural Analyst's Review Report:

1. Site design and conditions:
   a. New construction:
      (1) Placement of buildings and parking
      (2) Erosion containment and drainage
   b. Substantial Rehabilitation: Detail Work Write-up regarding:
      (1) Site utilities
      (2) Roads, walks, parking
      (3) Site improvements
      (4) Erosion containment and drainage
   c. Accessibility for persons with disabilities (If required by program or local code):
      (1) From street to residential and non-residential building(s)
      (2) From parking lot(s) to residential and non-residential building(s)
      (3) Throughout site
      (4) Any noncompliance of Fair Housing Act requirements for Substantial Rehabilitation projects constructed after March 13, 1991.

If unacceptable, indicate reasons:

2. Building design and conditions (include Detail Work Write-up for Substantial Rehabilitation):
   a. Fire safety

b. Accessibility for persons with disabilities - residential and non-residential structures for common use according to Fair Housing Act's specifications about design and construction, including but not limited to accessible public and common areas. See 42 U.S.C. § 3604(f)(3)(C)(i) – (iii). (For Substantial Rehabilitation projects only if required by program or local code):

(1) Circulation and community spaces

(2) Offices and other public spaces

(3) Typical residential units

If unacceptable, indicate reasons:

C. Review of A/E portion of completed Form HUD-92264for accuracy with respect to A/E exhibits (Include Detailed Work Write-up for Substantial Rehabilitation projects):

If unacceptable, indicate reasons:

D. Review of A/E exhibits for consistency with Lender's Review Report (Include Detailed Work Write-up for Substantial Rehabilitation projects):

1. Site work (and site elevations for new construction):

If unacceptable, indicate reasons:

2. Soils investigation and report and foundation design and placement (new construction):

If unacceptable, indicate reasons:

3. Residential and non-residential structures:

If unacceptable, indicate reasons:

4. Accessibility for persons with disabilities (Compliance with the Fair Housing Act's design and construction requirements is mandatory.) (For Substantial Rehabilitation projects only if required by program or local code):

a. From street and parking lots to residential and non-residential buildings.

b. Throughout site.

c. Throughout residential and common non-residential structures and spaces.

If unacceptable, indicate reasons:

5. Design features unusual for the particular structure type and/or system.

If unacceptable, indicate reasons:

6. Utility analysis if required by Hub Director at Pre-application review.

If unacceptable, indicate reasons:

7. Review reserve-for-replacement analysis where the formula has been waived.
   If unacceptable, indicate reasons:

E. Other A/E exhibits (indicate):
   If unacceptable, indicate reasons:

I have reviewed the subject project and hereby make the following recommendation(s):

Reviewer:

Name of Reviewer _____

Signature and Date of Review _____ Date _____

Concurrence:

Name of Team Leader _____

Signature and Date of Concurrence _____ Date _____

HUD Architectural Review of Lender's Architectural Analyst's Report for Firm Exhibits - Section 223(f)

5F.2

HUD Office Name _____

Firm Commitment Submission Date _____

Project Name _____

Project Location (City, State) _____ , _____

MAP Lender Name _____

NOTE: The following instructions apply to any housing receiving direct Federal assistance, such as Project-Based Section 8

Uniform Federal Accessibility Standards (UFAS) Requirements:

Although UFAS requirements technically apply only to new construction and alterations to existing buildings, the Department still requires addressing UFAS requirements on refinance transactions. This is true even though most repairs under Section 223(f) would not meet the definition of "alteration" as indicated in UFAS.

Summary of HUD Architectural Review

A. Firm Commitment deliverables:
   1. Lender's Project Capital Needs Assessment and Replacement Reserve Escrow (PCNA) Report
   2. Lender's review of PCNA Report
   3. Completed Form HUD-92264 with signatures

   If incomplete, specify:

B. Lender's Review of PCNA Report:
   1. Physical Inspection Report (PIR):
      a. Condition of project
      b. Project's:
         (1) Immediate repair needs
         (2) Expected repair, replacement, and major maintenance needs

If unacceptable, indicate reasons:

2. Statement of Resources and Needs
   a. Lender review/adjustment to PIR
   b. Critical repairs and non-critical repairs to be completed before endorsement
   c. Non-critical repairs to be completed after endorsement

If unacceptable, indicate reasons:

3. Accessibility for persons with disabilities (for projects constructed after March 13, 1991):
   a. From streets and parking lots to residential and non-residential building(s)
   b. Throughout site
   c. Residential and non-residential structures for common use:
      (1) Circulation and community spaces
      (2) Offices and other public spaces
      (3) Typical residential units
   d. Any noncompliance of Fair Housing Act requirements for projects constructed after March 13, 1991.

If unacceptable, indicate reasons:

C. Review of A/E portion of completed Form HUD-92264 for accuracy with respect to Lender's PCNA Report:

If unacceptable, indicate reasons:

D. Review of A/E exhibits for consistency with Lender's PCNA Report:
   1. Critical repairs

If unacceptable, indicate reasons:

2. Accessibility for persons with disabilities (Refer to the Fair Housing Act's specifications on design and construction, including but not limited to accessible public and common areas. See 42 U.S.C. § 3604(f)(3)(C)(i) – (iii)):
   a. From street and parking lots to residential and non-residential buildings
   b. Throughout site
   c. Throughout residential and common non-residential structures and spaces.

If unacceptable, indicate reasons:

I have reviewed the subject project and hereby make the following recommendation(s):

Reviewer:

Name of Reviewer _____

Signature and Date of Review _____ Date _____

Concurrence:

Name of Team Leader _____

Signature and Date of Concurrence _____ Date _____

Project Capital Needs Assessment

5G

I. WHAT IS A PROJECT CAPITAL NEEDS ASSESSMENT?

A Project Capital Needs Assessment (PCNA) defines what a Project's immediate and long term capital needs are and provides a plan for financing the capital needs. It consists of several components:

- The Physical Inspection Report;
- Lender Review of Physical Inspection Report;
- Lender Computation of Replacement Reserve Account;
- Lender Statement of Resources and Needs.

These are described separately below; HUD Review is also described.

II. THE PHYSICAL INSPECTION REPORT (PIR)

A. The Lender hires a "Needs Assessor" to prepare a PIR on the Project.

1. A Needs Assessor is any firm or individuals, including the Lender's architectural and cost analysts, qualified by training and experience to evaluate building systems and site conditions and to provide cost estimates.

2. The Needs Assessor and its Subcontractors participating in the preparation of the PIR may not have an Identity of Interest with the Mortgagor, sponsor, and managing agent (if any) of the proposed Project. An arms-length relationship is essential.

B. The PIR describes the current and future physical needs of the proposed multifamily Project. The PIR supplies the Lender and HUD with detailed information regarding:

1. The condition of the Project.
2. An identification of the Project's:
   a. Immediate critical and non-critical repair needs;
   b. Expected component replacement and major maintenance needs;
   c. Compliance with accessibility laws for persons with disabilities (for projects built after March 13, 1991).
3. The total estimated cost, adjusted for inflation, for all repair, component replacement and major maintenance items.

C. PIR Format:

1. Cover Sheet must include:
   a. The Project name, number and location.

b. Name, address, and telephone number of the preparer(s).

2. Table of Contents.
3. Project description.
4. Project Inspection Report(s) indicating existing conditions.

   NOTE: For multiple building projects, the Project Inspection Report must be itemized for each building. This is necessary to allow HUD to conduct backup inspections.

5. Repair Work Write-Up indicating scope of repairs:

   NOTE: For multiple building projects, the Repair Work Write-Up must be itemized for each building. This is necessary to permit the HUD inspector to conduct efficient and accurate inspections of the completed repair work.

   a. "Critical" (health and safety) repairs to be completed by initial/final endorsement of the mortgage;
   b. "Non-critical" repairs which may be deferred (subject to approval by the Hub or HUD Program Center Office) until after endorsement, but which must be completed within 12 months thereafter.
   c. Fair Housing Act compliance-related modifications and retrofits.

      This applies to all properties available for first occupancy after March 13, 1991, that do not fully comply with the Fair Housing Act design and construction requirements. These properties must be brought into compliance with the Fair Housing Act as a condition of insurance. This includes the scope of all modifications/retrofits needed to ensure that a property fully meets the design and construction requirements of the Fair Housing Act.

   d. Owner-proposed repairs and/or improvements. Such repairs and/or improvements must enhance the competitive value of the property in the marketplace to be acceptable. The cost of such repairs and/or improvements must not propel the total repair and improvement costs into the threshold of substantial rehabilitation. Examples are improvements to exterior and interior finishes and small additions to the structure, such as a covered entry or a small public sunroom. Such repairs and/or improvements shall be categorized as Non-Critical repairs.

6. Component replacement and major maintenance schedule(s). Prepare all schedules according to the following format:

   a. "Near Term" from the initial/final endorsement through the tenth year of the mortgage.
   b. "Long Term" from the eleventh through the twentieth year of the mortgage.
   c. "Remainder" from the twenty-first year until about two years beyond the maturity date of the Note and Mortgage.

7. Cost Estimate(s):

a. The cost of "critical" (health and safety) and "non-critical" repairs.

b. The cost of all modifications/retrofits needed to ensure that a property fully meets the design and construction requirements of the Fair Housing Act.

   1. Hard costs. Include the cost of all construction items for "critical" and "non-critical" repairs, and Fair Housing Act compliance-related modifications/retrofits. When estimating the cost of construction items that will require temporary relocation of residents, the Needs Assessor must develop a work schedule for these items that will efficiently utilize labor crews and provide for smooth turnover of temporary accommodations for each resident or residents in turn.

   2. Relocation costs. In the process of developing a scope of work for repairs and modifications/retrofits, the Needs Assessor must consider whether the proposed work will require the temporary relocation of residents while certain work items are being done. If temporary relocation is determined to be necessary, the Needs Assessor, using the work schedule, must estimate a relocation schedule and an overall relocation time, and develop a separate cost estimate for relocation to appropriate housing. The estimated relocation costs should be listed separately from the construction repair and modification/retrofit costs when developing the cost estimate for "critical" and "non-critical" repairs and Fair Housing Act compliance-related modifications/retrofits.

c. Owner-proposed improvements. The cost of such improvements must not propel the total repair and improvement costs into the threshold of substantial rehabilitation.

d. The Initial Deposit to the Reserve for Replacement Account and the Annual Deposit to the Reserve for Replacement Account based on the cost of "Near Term" replacement and major maintenance needs of the Project.

e. The cost of "Long Term" replacement and major maintenance needs of the Project.

f. The cost of "Remaining Term" replacement and major maintenance needs of the Project.

8. Engineering and Specialty Reports.

9. Standard size color photographs necessary to illustrate the conditions discussed in the report and a narrative describing each photograph.

D. Conducting the Inspections.

   1. The Needs Assessor may find it desirable to subcontract with other entities or persons for portions of the Project's physical inspection. For example, the Needs Assessor may wish to engage the services of a roofing subcontractor to furnish a roof inspection, a paving subcontractor to inspect the parking lots and sidewalks, a plumbing subcontractor to inspect the plumbing system, etc.

   2. The Department is leaving the working details of these arrangements to the Lender and the Needs Assessor hired by the Lender.

   3. The Needs Assessor must inspect enough dwelling units to be able to formulate an

accurate estimate of repair, replacement and major maintenance needs.

a. In some cases, depending on the size and condition of the Project, all or nearly all units will need to be inspected by the Needs Assessor.

b. In other cases, a lesser number of units may need to be inspected by the Needs Assessor.

c. The Department expects that appropriate statistical sampling methods and techniques will be used by the Needs Assessors to reach their conclusions about repair needs.

E. Estimating Repair, Replacement and Major Maintenance Needs Costs.

Regardless of the inspection procedures used, the final cost estimates of repairs, replacements and major maintenance items should be as accurate as practical in terms of present dollar values. The present dollar values will then be trended for future scheduled work using a reasonable inflation factor supplied by the Lender.

1. The Needs Assessor should assume that the Project will be in a better than "Satisfactory" condition when the Project's Note and Mortgage is paid off.

   a. This assumption is made explicit only for the purpose of standardizing or normalizing the data that will be furnished by the Department.

   b. Assume the Project to be in such a financial and physical condition that no unfunded major capital repairs would be anticipated for a period ending about two years after the maturity date of the Note. In other words, the PIR should not anticipate that the buildings would be run down or in need of the unfunded major repairs as of the maturity dates of their Notes and Mortgages.

2. The Department realizes that these long term estimates are projections that are subject to change.

F. Projections of Repairs, Replacements and Major Maintenance Costs. The Needs Assessor itemizes repairs, replacements, and major maintenance needs and breaks out the estimated dates by year that repairs, replacements and major maintenance needs will be needed according to the following format:

1. "Critical" [health and safety] repairs (to be completed before initial/final endorsement of the mortgage), "non-critical" repairs (which may be completed after initial/final endorsement of the mortgage), and Fair Housing Act compliance-related modifications and retrofits. In addition to all other critical repairs, the following items must be addressed:

   a. Accessibility for persons with disabilities (for properties constructed after March 13, 1991). The report must state whether the project appears to be in compliance with the Fair Housing Act and any other applicable accessibility laws. All noncompliance discovered must be reported in detail. Properties with Fair Housing Act noncompliance must be modified/ retrofitted. See II.C.7.

   b. Abatement of lead-based paint (LBP) and asbestos. This applies to all existing

properties constructed prior to 1978 which have not been demonstrated to be LBP- and/or asbestos-free. For projects that contain LBP and/or asbestos, the Needs Assessor is responsible for engaging the services of a qualified LBP and/or asbestos abatement contractor(s) to prepare a scope of work for the abatement of LBP and/or asbestos. Where the scope of abatement work consists of permanent enclosure or encapsulation, but not removal, of LBP and/or asbestos, the qualified abatement contractor(s) must also prepare, separate from the scope of abatement work, an Operations and Maintenance (O&M) Plan for LBP and/or asbestos. The O&M Plan contains ongoing maintenance activities for LBP and/or asbestos, to be followed for as long as the LBP and/or asbestos remains in place. All abatement work and ongoing maintenance activities for LBP and/or asbestos shall conform to the following Regulatory requirements:

(1) For LBP, 24 CFR Part 35;

(2) For asbestos, 40 CFR Part 61.

For Lender certification requirements, see Section III.C.

c. Items of deferred maintenance: Defined as "Postponed, infrequent or inadequate maintenance practices on a building or property, often resulting in physical depreciation and loss of value." Conditions that should have been prevented or repaired as part of a previous year's (or multiple years') project maintenance program are considered deferred maintenance. Items that coincidentally become necessary at the time of underwriting are not considered deferred maintenance.

(1) Where such items bring about a condition(s) that requires a Critical Repair(s), all such repairs must be completed before initial/final endorsement.

(2) Where the condition(s) requires non-critical repairs, if the project is being processed as:

(a) A refinance transaction, the items must be completed before initial/final endorsement of the mortgage.

(b) A purchase transaction, the items may be included in the non-critical repairs list to be completed after initial/final endorsement.

d. Seismic repairs: Seismic repairs under the 223(f) program should be treated as non-critical unless there are circumstances that warrant otherwise.

2. Replacements and Major Maintenance Schedule:

The Needs Assessor will prepare a schedule to estimate the remaining useful life of all short-lived building components and equipment included in the Project. The Remaining Useful Life estimate must come from a nationally recognized source such as "Marshall and Swift." The schedule will be itemized according to the three main categories defined above:

a. "Near Term",

b. "Long Term", and

c. "Remainder".

III. LENDER REVIEW OF THE PHYSICAL INSPECTION REPORT

The Lender reviews the PIR and makes any appropriate adjustments as indicated below.

A. The Lender's review is to determine whether:

1. The PIR covers the appropriate mortgage term;
2. All items requiring action during the mortgage term are included in the PIR;
3. An adequate sampling of units was made, and management reported replacements have been verified and considered;
4. Appropriate ages are given for individual elements and whether any deviations from the expected useful lives are adequately justified; and
5. The PIR contains any material mathematical errors.

B. Some items identified in the PIR may be part of the current operating budget for the Project.

1. If these items (such as replacement of garbage disposals or smoke detectors) are included in the normal operating budget for the Project, funds for their maintenance or replacement should not be included in the Replacement Reserve.
2. The Lender should only remove such items from the Needs Assessor's estimate if there is clear evidence that the operating budget for the Project includes these items and the items are of relatively nominal cost.
3. The Lender should also ensure, in the review of prior operating statements for the Project, that any "capital" items deleted from the maintenance line items are addressed in the calculation of reserves if they are likely to recur during the term covered by the PCNA.

C. The Lender should review the PIR to assure that all items indicated below are appropriately listed, and the Needs Assessor's cost estimates and projected dates of completion are reasonable.

1. Review all repair, replacement or major maintenance items that could potentially impact the health or safety of residents (e.g., installation of exit lighting at a basement exit), or that violate applicable codes; these should be listed as Critical Repairs to be completed before initial/final endorsement.

   a. For projects that contain Lead Based Paint (LBP) and/or asbestos where the LBP and/or asbestos abatement does not involve removal:

      (4) The Lender must certify that the Needs Assessor has prepared an Operations and Maintenance (O&M) Plan and that the Plan will remain in effect for the life of the mortgage.

(5) A certification from the Lender to this effect is a mandatory condition for Firm Commitment and a required exhibit at Initial/Final Closing.

2. Review all other repair, replacement or major maintenance items not included in the operating budget. Included in this category are any items that are necessary to:
   a. Correct any deferred maintenance;
   b. Prevent physical deterioration of the Project; and
   c. Correct conditions that decrease the marketability of the Project (e.g., items of functional obsolescence.)
      3. The Lender must determine the dates for the completion of all work.
   a. These completion dates must be appropriate for the significance of the work being done.
   b. However, in all events, the critical repairs must be completed before, and non-critical repairs no later than 12 months after, initial/final endorsement.

D. The Lender should review the PIR to ascertain that the number of years over which replacements and major maintenance items are expected to occur represents a reasonable conclusion and that the Needs Assessor's cost estimate is reasonable and adequate to address the Project's needs. The Lender should ensure that the Needs Assessor has not:
   1. Estimated costs based on the worst case (e.g., replacement of all aging refrigerators in a single year).
   2. Been unduly optimistic in determining the schedule or costs (e.g., replacement of only a small percentage of refrigerators per year such that replacements exceed life expectancy or are stretched beyond the term of the Mortgage without justification).

E. Completion of Repairs:

   The Lender is expected to exercise independent judgment when recommending which items must be completed before initial/final endorsement and which items are non-critical items that may be completed after initial/final endorsement.
   1. At initial/final endorsement of the mortgage, the Project shall not have any conditions that threaten the health or safety of residents.
   2. Non-critical repairs may be completed after initial/final endorsement (with concurrence of the Department).

IV. COMPUTATION OF THE REPLACEMENT RESERVE ACCOUNT BY THE LENDER.

The Needs Assessor prepares an analysis of the remaining useful life of short-lived building components and systems, and other Project features. Lender uses this to evaluate the adequacy of the replacement reserve account and any necessary initial deposit to that account.

A. Ineligible items.
   1. Items generally considered routine maintenance shall not be included in the calculation

of the Replacement Reserve Account.

2. Items involving any repairs, rehabilitation or construction shall **not** be included in the Replacement Reserve Account.

B. Remaining useful life:

1. To derive the remaining useful life of an item, subtract the actual age of the item from the estimated economic life of the item.
2. The schedule shall provide a description of the item, actual age and estimated economic life of the item.

C. Reserve for Replacement Account for Near Term items:

The Lender must, in the Statement of Resources and Needs, determine and recommend to HUD the Total near Term Reserve for Replacement Account for the Project.

To provide for anticipated Near Term replacements and major maintenance needs, prepare a 100 percent replacement cost estimate (less salvage) for each item in the group whose estimated remaining useful life is expected to expire in the first ten years.

1. Include the sum of the costs of labor/installation, materials, and appropriate fees, when applicable. Using a cost adjustment factor for inflation, project the cost of each item from the date (month and year) of the estimate to the expected expiration date. The sum of the estimated cost is the Total Near Term Reserve for Replacement Account, which includes the initial deposit and the annual deposits required from the Mortgagor.
   a. The Total Near Term Reserve for Replacement Account must be at least equal to the total estimated cost (adjusted for inflation) of completing the items shown in the Near Term replacement and major maintenance needs schedule of the Project.
   b. The total deposits by the Mortgagor in the Near Term Reserve for Replacement Account should equal the Total Near Term Reserve for Replacement amount.
   c. If the Mortgagor is required to make an initial deposit into the Reserve for Replacement, the Lender may subtract the amount of the initial deposit from the Total Near Term Reserve for Replacement amount in determining the amount of the monthly deposits to the Reserve for Replacements to be made by the Mortgagor.
2. Davis-Bacon Requirements do not apply and, therefore, the costs of labor shall <u>not</u> include the provisions of Davis-Bacon.
3. Identify the location of items, if required for clarification.
4. The Total Near Term Reserve for Replacement Account must be at least equal to $150 per unit, per annum.

D. Evaluation of the Reserve Account for Long Term and Remainder items:

1. An additional evaluation must be made by the Lender every ten years to determine whether annual deposits to the reserve account are sufficient (See VI.C).

2. The Lender must address how later adjustments in the annual deposit will be made and the financial risk to HUD.

E. Funding Schedules for Near Term, Long Term, and Remainder items in the Reserve for Replacement Account.

The Lender's Statement of Resources and Needs must set forth a funding schedule for the entire mortgage term, and demonstrate that the funding schedule shows that money will be there yearly to meet the physical needs of the Project and the overall underwriting of the loan.

The Lender recommends to HUD the appropriate funding structure for Near Term, Long Term, and Remainder items in the Reserve for Replacement, based on the timing of the expected replacements, and/or whether the Mortgagor will receive cash upon closing the Mortgage. If HUD accepts the Lender's recommendation, the funding schedule (along with the requirement for a re-evaluation every ten years) will be inserted into the Regulatory Agreement by HUD.

The following are examples of alternative funding schedules:

1. No initial deposit and large monthly deposits because the repairs and replacements are concentrated in the later years of the Mortgage term.
2. Monthly deposits that increase over the term of the Mortgage (e.g., payments which increase 5 percent per year over the term of the Mortgage) to match the estimated timing of repairs and replacements may be appropriate in some instances.

Note: If there is no initial deposit, a disproportionately small monthly deposit in the first year, designed to reduce the impact on underwriting, is unacceptable.

V. STATEMENT OF RESOURCES AND NEEDS.

The Lender's statement must:

A. Address the quality of the PIR; and

B. Discuss any adjustment made to the PIR by the Lender.

C. Identify the replacement and major maintenance items for which the owner may be reimbursed from the Replacement Reserve.

Note: HUD will only disburse funds for those replacement or major maintenance items specifically listed in the Statement.

D. Recommend to HUD the dollar amount of:

1. The cost of repairs to be completed before initial/final endorsement of the mortgage.
2. The cost of, and the amount to escrowed for, non-critical repairs to be completed within one year of date of initial/final endorsement of the mortgage.
3. Initial deposit, if any, and the amount of the monthly deposits and the funding schedule of such deposits into the Replacement Reserve based on "Near Term" projections of

replacement and major maintenance costs.

E. Describe:

1. Current financial or other assistance needs and resources of the Project.
2. Future financial or other assistance needs and resources. Specifically how "Long Term" and "Remainder" projected replacement and major maintenance costs will be covered.

VI. HUD REVIEW.

A. The HUD Office should:

1. Review the PCNA for completeness and adequacy. The review should include a careful examination of the Department's long-term risk associated with non-traditional calculation of annual deposits to the replacement reserve.
2. Discuss all weaknesses or inadequacies of the PCNA with the Lender in an effort to reach consensus about the needs and resources of the project. The results of these discussions and agreements reached must be incorporated into the firm commitment and loan closing documents.

B. If the HUD Office determines that a PCNA is substantially incomplete or inadequate:

1. Notify the Lender of the portion(s) of the PCNA that require completion or revision and require the Lender to submit an amended PCNA within thirty (30) days from receipt of the Field Office's notification.
2. If HUD and the Lender fail to reach closure, HUD will impose its own methodology for computation of annual deposit to the replacement reserve.

C. The Lender will recommend and HUD may set up the Total Near Term Replacement Reserve Account.

1. HUD will reevaluate the Project's Replacement Reserve needs and, if appropriate, adjust the Mortgagor's required deposits to the Replacement Reserve every ten years.
   a. To assist in completing this evaluation, the Lender must obtain a new PCNA every 10 years which covers the next ten years [or the remaining term of the Mortgage] plus two years.
   b. Replacement Reserve funds may be used to pay for the additional PCNAs.
2. The Hub or Program Center at the time of initial/final endorsement will have a rider signed by the Lender and HUD and attached to the Lender's Certificate which will require the Lender to comply with the requirements of C.1 above.

Design Architect's Certification

5H

HUD Project Name

HUD Project Number

Mortgagor

I, the undersigned Design Architect, to the best of my knowledge, belief and professional judgment, hereby certify that the proposed construction in accordance with the working drawings and specifications prepared for the subject Project (a) is permissible under the applicable zoning, building, housing, and other codes, ordinances and/or regulations, as modified by any waivers obtained from appropriate officials, and (b) complies with the HUD Minimum Property Standards, applicable accessibility laws for persons with disabilities, and other applicable HUD Standards, guidelines and criteria.

Waiver of codes etc., were obtained as listed in attachment (identify):

Signed by _____

Date _____

Architect's Name _____

Business Address _____

License Number _____

Warning: Title 18 U.S.C. 1001, provides in part that whoever knowingly and willfully makes or uses a document containing any false, fictitious, or fraudulent statement or entry, in any manner in the jurisdiction of any department or agency of the United States, shall be fined not more than $10,000 or imprisoned not more than five years or both.

Certificate of Professional Liability Insurance

5H.1

HUD Project Name

HUD Project Number

Mortgagor

To: Mortgagee and Secretary of Housing and Urban Development

I certify that _____(Name of Architect/ Engineer/ Design Professional) is insured in the amount of $_____ under _____(Name of Insurer) Policy No. _____ of Architect and/or Engineers Professional Liability Insurance.

This Policy shall be maintained up through acceptance of the 12-month warrantee inspection for the subject HUD Project.

Signature _____

Title _____

Date _____

Insurer's Name _____

Business Address _____

_____

Warning: Title 18 U.S.C. 1001, provides in part that whoever knowingly and willfully makes or uses a document containing any false, fictitious, or fraudulent statement or entry, in any manner in the jurisdiction of any department or agency of the United States, shall be fined not more than $10,000 or imprisoned not more than five years or both.

Appendix 6

Cost Analysis

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[redacted] Cost Processing

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HUD Cost Review Report for Pre-Application Exhibits

6A.1

HUD Office Name _____

Pre-Application Submission Date _____

Project Name _____

Project Location (City, State) _____

MAP Lender Name _____

Summary of HUD Cost Review

A. Cost exhibits:
   1. Mortgagor's Architect's sketch plans
   2. Form HUD-92013

      If incomplete, specify:

B. For Substantial Rehabilitation projects, include the following:
   1. Mortgagor's Architect's Basic Work Write-up
   2. Mortgagor's summary cost estimate for substantial rehabilitation (based on Basic Work Write-up)

      If incomplete, specify:

C. HUD Cost Estimator determination of:
   1. Structure type (from sketch plans):
   2. Gross floor area (from sketch plans):
   3. Estimated Total Structures cost (from cost data):
   4. For Substantial Rehabilitation, indicate major trade item groups (if required), and subtotals:
   5. Estimated Total Land Improvements cost (from cost data):
   6. Estimated General Requirements (from cost data):
   7. Estimated fee items (from cost data):
      a. General Overhead
      b. Builder's Profit
      c. Architectural Fees
      d. Bond Premium

e. Other Fees

D. Review of mortgagor's Form HUD-92013:

1. Percentage difference between mortgagor's Total Structures cost (Section G, Line 8) and HUD Cost Estimator's Total Structures cost:

   If unacceptable, document:

2. Percentage difference between mortgagor's Total Land Improvements cost (Section G, Line 3) and HUD Cost Estimator's Total Land Improvements cost:

   If unacceptable, document:

3. Percentage difference between mortgagor's General Requirements and fees (Section G, Lines 10 through 19) and HUD Cost Estimator's General Requirements and fees:

   If unacceptable, document:

I have reviewed the subject project and hereby make the following recommendation(s):

Reviewer:

Name of Reviewer _____

Signature and Date of Review _____ Date _____

Concurrence:

Name of Team Leader _____

Signature and Date of Concurrence _____ Date _____

HUD Cost Review of Lender's Cost Analyst's Report for Firm Exhibits – New Construction and Substantial Rehabilitation

6A.2

HUD Office Name _____

Firm Commitment Submission Date _____

Project Name _____

Project Location (City, State) _____

MAP Lender Name _____

Summary of HUD Cost Review

A. Firm Commitment deliverables (Review for completeness only):

1. Mortgagor's:
   a. Detailed plans and specifications
   b. Detail Work Write-up (For substantial rehabilitation projects)

   If incomplete, specify:

2. Lender's Cost Analyst's Review Report:
   a. Lender's detailed cost estimate
   b. Comparison of Lender's and general contractor's cost estimates
   c. Prior approval of Identity of Interest subcontracts
   d. Property Insurance schedule
   e. For substantial rehabilitation projects, include the Lender's estimate for Annual Deposit to the Replacement Reserve.

   If incomplete, specify:

3. Completed Forms with signatures:
   a. HUD-92264
   b. HUD-92326
   c. HUD-92331-B
   d. HUD-92329
   e. HUD-2328

   If incomplete, specify:

4. Subcontracts for Identity of Interest subcontractors

   If incomplete, specify:

B. HUD Cost Review:

1. Comparison of Lender's cost estimate and contractor's HUD-2328 with HUD cost data:
   a. Total Structures
   b. Total Land Improvements
   c. General Requirements
   d. Fee items
   e. Cost Not Attributable items

   If unacceptable, document:

2. Examination of Lender-contractor variance report (Form HUD-2331-B)

   If unacceptable, document:

3. Examination of:
   a. Identity of Interest relationships
   b. Applications for prior approval of Identity of Interest subcontractor overhead and profit

   If unacceptable, document:

4. Examination of Property Insurance Schedule

   If unacceptable, document:

   If unacceptable, document:

I have reviewed the subject project and hereby make the following recommendation(s):

Reviewer:

Name of Reviewer _____

Signature and Date of Review _____ Date _____

Concurrence:

Name of Team Leader _____

Signature and Date of Concurrence _____ Date _____

HUD Cost Review of Lender's Report for Firm Exhibits - Section 223(f)

6A.3

HUD Office Name _____

Firm Commitment Submission Date _____

Project Name _____

Project Location (City, State) _____

MAP Lender Name _____

Summary of HUD Cost Review

A. Firm Commitment deliverables:
   1. Lender's Project Capital Needs Assessment and Replacement Reserve Escrow (PCNA) Report
   2. Completed Form HUD-92264 with signatures
   3. Completed Form HUD-92329

   If incomplete, specify:

B. HUD Cost Review:
   1. Examination of Lender's PCNA Report:
      a. Critical repairs to be completed before endorsement
      b. Non-critical repairs to be completed after endorsement and estimated repair costs
      c. Expected repair replacement and major maintenance items over a specified period of time
      d. Initial Deposit to Replacement Reserve, if any
      e. Monthly Deposit to Replacement Reserve

      If unacceptable, document:

   2. Lender's Property Insurance Schedule

      If unacceptable, document:

I have reviewed the subject project and hereby make the following recommendation(s):

HUD Office Name _____

Project Name _____

Project Location (City, State) _____

MAP Lender Name _____

Amendment to the Construction Contract to Identify Identities of Interest Between Owner/ Contractor/ Subcontractors/ Architect

6B

Project Name _____ Project Number_____

1. Definition of terms used in this Amendment.
   a. Architect. Architect administering the Construction Contract.
   b. HUD. The U.S. Department of Housing and Urban Development.
   c. Owner. The Mortgagor/Owner.
   d. Subcontractor. Any Project subcontractor, materials supplier, equipment lessor, or industrialized housing manufacturer/supplier.
2. The undersigned hereby certify that all identities of interest known to exist between the Owner and the Contractor, and/or between the Owner and/or the Contractor and the Architect and/or any Project subcontractor are listed herein. The Owner and the Contractor shall each inform HUD in writing within 5 working days of its knowledge of any identity of interest that develops after execution of this Contract.

   List all Identities of Interest:

   _____

   _____

   _____

   _____

   _____

   _____

3. An Identity of Interest is construed to exist where:
   a. The Contractor, Architect and/or any subcontractor take any financial interest in the Project and/or Owner as part of the consideration to be paid.
   b. The Contractor advances any funds to the Owner or Architect; or the Architect advances any funds to the Owner, contractor and/or any subcontractor; or any subcontractor advances any funds to the Owner, Contractor and/or Architect.
   c. The Owner has any financial interest in the Contractor, Architect and/or any subcontractor; or the contractor has any financial interest in the Owner, Architect and/or any subcontractor; or the Architect has any financial interest in the Owner, Contractor and/or any subcontractor; or any subcontractor has any financial interest in the Owner, Contractor and/or Architect.

d. Any officer, director, stockholder or partner of the Owner has any financial interest in the Contractor, Architect and/or any subcontractor; or any officer, director, stockholder or partner of the Contractor, has any financial interest in the Owner, Architect and/or any subcontractor; or any officer, director, stockholder or partner of the Architect has any financial interest in the Owner, Contractor and/or any subcontractor; or any officer, director, stockholder or partner of any subcontractor has any financial interest in the Owner, Contractor and/or Architect.

e. Any officer, director, stockholder or partner of the Owner is also an officer, director, stockholder or partner of the Contractor, Architect and/or any subcontractor; or any officer, director, stockholder or partner of the Contractor is also an officer, director, stockholder or partner of the Owner, Architect and/or any subcontractor; or any officer, director stockholder or partner of the Architect is also an officer, director, stockholder or partner of the Owner, Contractor, and/or any subcontractor; or any officer, director, stockholder or partner of any subcontractor is also an officer, director, stockholder or partner of the Owner, Contractor and/or Architect.

f. The Owner, Contractor and/or any subcontractor, or any officer, director, stockholder or partner of such Owner, Contractor and/or subcontractor provides any of the required architectural services; or where the Owner, Contractor and/or any subcontractor, or any officer, director, stockholder or partner of such Owner, Contractor and/or subcontractor, while not directly providing an architectural service, acts as a consultant to the Architect.

g. Any family relationships between the officers, directors, stockholders or partners of the Owner and officers, directors, stockholders or partners of the Contractor, Architect and/or any subcontractor; or between the officers, directors, stockholders or partners of the Contractor and officers, directors, stockholders or partners of the Owner, Architect and/or any subcontractor; or between any officers, directors, stockholders, or partners of the Architect and officers, directors, stockholders or partners of the Owner, Contractor and/or any subcontractor; or between any officers, directors, stockholders or partners of any subcontractor and the officers, directors, stockholders or partners of the Owner, Contractor and/or Architect which could cause or results in control or influence over prices paid and/or work accepted.

h. Any side deal, agreement, contract or undertaking, thereby altering, amending, or canceling any of the required closing documents, except as approved by HUD.

OWNER	CONTRACTOR
_____	_____
_____	_____
DATE _____	DATE _____

WARNING: Title 18 U.S.C. 1001, provides in part that whoever knowingly and willfully makes or uses a document containing any false, fictitious, or fraudulent statement or entry, in any matter in the jurisdiction of any department or agency of the United States, shall be fined not more than $10,000 or imprisoned for not more than five years or both.

Rehabilitation Cost Not Attributable to Residential Use

6C

Steps 1 through 8 of this Worksheet are intended for determining Rehabilitation Cost Not Attributable (CNA), and "As-Is" CNA, for building structures. If the building structure contains a parking garage within its footprint, the cost and floor area of the garage should be included in Steps 1 through 8. In addition, if the property contains a CNA use within an enclosed building that is separate from the residential structure(s), e.g. a small community building, the cost and floor area of such a CNA use should be included in Steps 1 through 8.

However, if there is no parking garage, but rather an open-air parking lot (and/or other open-air non-attributable use, such as a tennis court) separate from the building, the following procedure should be used:

1. The cost to rehabilitate the parking lot (and/or other open-air use) should be included in Total Rehab Cost (Step 1) and Rehab Cost Not Attributable (Step 2).
2. However, the area of the parking lot (and/or other open-air use) should **not** be included in the Project Structures Not Attributable Square Feet nor the Total Project Structures Gross Square Feet (Step 3).
3. The area(s) of the parking lot (and/or other open-air use) will be entered in Step 9 and multiplied by the Estimated Value of Land without Improvements and divided by the area of the project site.
4. Step 10 adds the amount in Step 9 to the subtotal in Step 8, to arrive at a total Rehabilitation Cost Not Attributable to Residential Use.

See the Example in Appendix 6D.

Rehabilitation Cost Not Attributable to Residential Use Worksheet

1. Total Rehab Cost

(Without fees - Lines G 36c + G41 from HUD-92264) = $ _____

2. Rehab Cost Not Attributable*

(Dollar amounts without fees for Structures and Land Improvements) = $ _____

* From Cost Analyst

3. Ratio of Not Attributable*

Project Structures Not Attributable Square Feet (Structure(s) only) _____sq. ft.*

Divided by Total Project Structures Gross Square Feet (Structure(s) only) _____ sq. ft.* = _____ %

* From Cost Analyst

4. "As-Is" Not Attributable

Total "As-Is" Value $ _____ (From Line G.73b of Form HUD-92264)

X Ratio from #3 _____ % = $_____

5. Total Cost Not Attributable

"As-Is" Not Attributable (#4) $ _____

plus Rehab Cost Not Attributable (#2) $ _____ = $ _____

6. Total Cost Without Fees

Total Rehab Cost Without Fees $ _____ (From #1) plus

Total "As-Is" Value $ _____ (From Line G.73b of Form HUD-92264) = $ _____

7. The Percentage Not Attributable

Divide Total Cost Not Attributable (#5) $ _____

by Total Cost Without Fees (#6) $_____ = _____%

8. Rehab Cost Not Attributable for Project Structures

Total Estimated Replacement Cost of Project (Line G.74)

$ _____ X Percentage Not Attributable (#7) _____ % = $ _____

9. "As-Is" Not Attributable for Open Air Parking Lots and Other Open Air Uses

Total Open Air Non-Attributable Area _____ sq. ft.* X Estimated Value of Land Without Improvements $_____ divided by Site Area _____ sq. ft. = $_____

***** From Cost Analyst

10. Total Rehabilitation Cost Not Attributable to Residential Use

Add Rehab CNA for Project Structures (#8) $_____ and "As-Is" Not Attributable for Open Air Parking Lots and Other Open Air Uses (#9) $_____ = $_____

Examples of Calculating Cost Not Attributable for New Construction and Substantial Rehabilitation

6D

EXAMPLE OF CALCULATING COST NOT ATTRIBUTABLE FOR NEW CONSTRUCTION

A 50-unit apartment building has a gross floor area of 30,000 sq.ft. and a footprint of 7,200 sq.ft. It has a Total Structures cost of $1,665,000, and a Total Land Improvements cost of $250,000. It has a community room on the ground floor, a parking lot, an exterior patio with benches, tables, and ornamental shrubs, and a playground with swings and slides. Using the architectural drawings, determine the area of the community room, parking lot, patio, and playground, and the number of benches, tables, ornamental shrubs, swings and slides. Calculate the cost of each item.

Unit quantities:

Community room - 650 sq.ft.

Asphalt parking lot for 50 cars - 15,000 sq.ft.

Concrete Patio - 400 sq.ft.

Playground - 900 sq.ft.

6 ft concrete patio benches - 6

3 ft x 3 ft concrete patio tables - 6

Ornamental shrubs - 12

Playground swing sets - 2

Playground slides - 2

Unit costs:

A. The community room is part of the structure, while the rest of the non-attributable features are exterior. The unit cost for the community room will be the Total Structures cost per gross square foot of building area. In Form HUD -92264, divide $1,665,000 (Line 41 of Section G) by 30,000 sq.ft. (Line 33 of Section C), giving a cost per gross square foot of $55.50.

B. Determine unit costs for exterior features from the Office benchmark data bank or a published data source. The exterior unit costs used in this example are typical.

Parking lot:

Asphaltic concrete parking lot paving - $1.25 per sq.ft.

Concrete perimeter curbing (500 lin ft) - $10.50 per lin. ft.

Concrete parking bumpers - $30 ea.
Stormwater catch basins (4) - $1500 ea.
Storm drain line (350 lin ft) - $27 per lin. ft.
Parking lot striping - $4 per car

Patio:
Concrete patio paving - $4 per sq.ft.
Concrete patio benches - $500 ea.
Concrete patio tables - $1000 ea.
Ornamental shrubs - $100 ea.
Playground:
Asphalt paving - $2 per sq.ft.
Rubber safety surface - $3 per sq.ft.
Swing sets - $500 ea.
Slides - $1000 ea.

C. Cost Calculations:

1. "B" Costs:

These are summarized according to category in Section M of Form HUD-92264.

M.10 - Parking

Parking lot paving - 15,000 sq.ft. x 1.25	=	18,750
Parking lot curbing - 500 lin.ft. x 10.50	=	5,250
Parking bumpers - 50 x 30.00	=	1,500
Catch basins - 4 x 1500.00	=	6,000
Storm drain - 350 lin.ft. x 27.00	=	9,450
Striping - 50 x 4.00	=	200
Summary cost	=	41,150

M.13 - Special Exterior Land Improvements

Patio paving - 400 sq.ft. x 4.00	=	1,600
Patio benches - 6 x 500.00	=	3,000
Patio tables - 6 x 1000.00	=	6,000
Ornamental shrubs - 12 x 100.00	=	1,200
Playground paving - 900 sq.ft. x 2.00	=	1,800
Safety surface - 900 sq.ft. x 3.00	=	2,700
Swing sets - 2 x 500.00	=	1,000
Slides - 2 x 1000.00	=	2,000

Summary cost = 19,300

M.14 - Other

Community room - 650 sq.ft. x $55.50 = $36,075

Total Summary Costs = M.10 + M.13 + M.14 = **TOTAL "B" COSTS = $96,525**

Enter summary costs and breakdown in Section M.

2. "A" Costs

Total Structures (HUD-92264, line G.41)	= $1,665,000
Total Land Improvements (line G.36c)	= 250,000
TOTAL "A" COSTS	**= $1,915,000**

3. Cost Not Attributable (B over A):

"B" costs @ $96,525 divided by "A" costs @ $1,915,000 = 0.0504 = 5.04 percent

Enter the percentage in Section M of Form HUD-92264.

EXAMPLE OF CALCULATING COST NOT ATTRIBUTABLE FOR SUBSTANTIAL REHABILITATION

Apartment building containing community space and commercial space, a separate athletic club building, and an open-air parking lot.

Units: 50
Gross Floor Area: 50,000 sq ft (residential structure)
1,000 sq ft (athletic club building)
Total Site Area: 25,000 sq ft

Form HUD-92264 Section G

Rehab cost for Structures:	=	$1,020,000
Rehab cost for Land Improvements:	=	$125,000
Rehab Gen. Requirements an	=	$225,000
Soft Costs:		
Carrying Charges, Financing, Legal, Organizational, Audit	=	$400,000
Contingency Reserve	=	$100,000
"As-Is" Value:		
Structure: $3,000,000 (residential) + $50,000 (athletic club building) + Land: $500,000 (25,000 sq ft @ $20/sq ft)	=	$3,550,000
Total = Line G.74	=	$5,420,000

Non-attributable areas:

Residential Structure: Community Room @ 1000 sq ft
Commercial space @ 2000 sq ft
Athletic club building @ 1000 sq ft
Open air: Parking lot for 50 cars @ 15,000 sq ft

Rehab Cost Not Attributable (Without Fees):

Residential Structure: Community Room: 1000 sq ft @ $20/sq ft = $20,000
Commercial space: 2000 sq ft @ $30/sq ft = $60,000
Athletic club building (non-commercial): 1000 sq ft @ $20/sq ft = $20,000
Open Air: Patch and re-stripe parking lot:
15,000 sq ft @ $1/sq ft = $15,000

STEP A: B over A Test:

Non-commercial Uses:

Community Room: B = $20,000 (Rehab CNA)

Athletic club bldg: B = 20,000

Parking Lot B = 15,000

Total B = $55,000

A = $1,145,000 (Rehab cost for Structures plus Land Improvements)

Non-commercial B over A percentage

= $55,000/ 1,145,000 = 4.80 percent. **Acceptable.**

Commercial space:

Commercial B over A percentage

= $60,000/ 1,145,000 = 5.24 percent. **Acceptable.**

STEP B: Rehab CNA Worksheet:

Step 1. **Total Rehab Cost**

Land and Structures = **$1,145,000**

Step 2. **Rehab Cost Not Attributable**

= $20,000 + 60,000 + 20,000 + 15,000 = **$115,000**

Step 3. **Ratio of Not Attributable.**

USE ONLY THE AREAS WITHIN THE RESIDENTIAL STRUCTURE AND ENCLOSED NON-ATTRIBUTABLE BUILDINGS FOR PROJECT NOT ATTRIBUTABLE AND PROJECT GROSS SQUARE FEET.

Project Structures Not Attributable Square Feet

= 1,000 sq ft (community room)

Plus 2,000 sq ft (commercial)

Plus 1,000 sq ft (athletic club building)

Total = 4,000 sq ft

Project Structures Gross Square Feet

= 50,000 sq ft (Gross Floor Area – Residential building)

Plus 1,000 sq ft (athletic club building)

Total = 51,000 sq ft

Ratio = 4,000 sq ft / 51,000 sq ft = 0.0784 = **7.84 %**

Step 4. **"As-Is" Not Attributable.**

Total "As-Is" (Land + Structures) = $500,000 + $3,000,000 + $50,000
=$3,550,000 X Ratio from Step 3 = 7.84% = **$278,320**

Step 5. **Total Cost Not Attributable.**

"As-Is" Not Attributable (#4) = $278,320 plus Rehab Cost
Not Attributable (#2) = $115,000 = **$393,320**

Step 6. **Cost Without Fees.**

Total Rehab Cost (Without Fees) (#1) = $1,145,000 +
Total "As-Is" Value (Land + Structures) = $3,550,000 = $**4,695,000**

Step 7. **The Percentage Not Attributable**.

Divide Total Cost Not Attributable (#5) = $393,320
by Cost Without Fees (#6) = $4,695,000 = **8.38 %**

Step 8. **Rehab Cost Not Attributable for Project Structures**.

Total Estimated Replacement Cost of Project (Line G.74) = $5,420,000
X Percentage Not Attributable (#7) = 8.38 % = **$454,196**

Step 9. **"As-Is" Not Attributable for Open Air Parking Lots and Other Open Air Uses**

Total Open Air Non-Attributable Area (parking lot) = 15,000 sq. ft.
X Estimated Value of Land Without Improvements = $500,000,
divided by Site Area = 25,000 sq. ft. = **$300,000**

Step 10. **Total Rehabilitation Cost Not Attributable to Residential Use**

Add Rehab CNA for Project Structures (#8) = $454,196 and
"As-Is" Not Attributable for Open Air Parking Lots and
Other Open Air Uses (#9) = $300,000 = **$754,196**

Appendix 7

Valuation Processing

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7A	HUD Appraiser Technical Review - Pre-Application Section 220, 221(d)(3), 221(d)(4), and 231
7B	HUD Appraiser Technical Review – Firm Commitment Section 220, 221(d)(3), 221 (d)(4) and 231
7C	HUD Appraiser Technical Review – Direct to Firm Commitment Section 220, 221(d)(3), 221(d)(4) and 231
7D	HUD Appraiser Technical Review – Firm Commitment Section 223(f)

HUD Appraiser Review – Review of Appraisal and Market Study HUD Valuation Report - Technical Review of Multifamily Accelerated Processing - Pre-Application Section 220, 221(d)(3), 221(d)(4) and 231

7A

This review of appraisal/consulting work product is to be completed in accordance with Standard 3 of the Uniform Standards of Professional Appraisal Practice (USPAP) currently in effect. The reviewer's client and intended user is the U. S. Department of Housing and Urban Development. The purpose of the review is to ascertain if the appraisal/consulting work product under review meets the applicable requirements of the USPAP and HUD, and that the work product has produced well-supported conclusions that can be relied on for the purpose of making a recommendation to issue, or not issue an invitation to apply for a Firm Commitment for HUD mortgage insurance.

HUD Multifamily Hub: _____

Team Leader: _____

Reviewer: _____

Date Received for Review: _____

Date of Reviewer Site Visit: _____

Review Report Completion Date: _____

SOA: _____ 220 _____ 221(d)(3) ____ 221(d)(4) _____ 231

Activity: (check all that apply) ____ New Construction ____ Sub-rehab ____ Acquisition ____ Refinance

Project Name: _____

Case #: _____

Mortgagee: _____

Mortgagor: _____

Appraiser: _____

Market Analyst: _____

Date of Report under Review: _____

Property and Ownership Interest Appraised: _____

Effective Date of Review: _____

A. Standard 3 Compliance:

1. The Reviewer was able to adequately identify the property that is the subject of this review.
   - ☐ Yes
   - ☐ No (Document)

2. The Reviewer inspected the exterior of the subject and the following units (if applicable, list)
   - ☐ Yes
   - ☐ No (Document)

3. The Reviewer inspected the exterior of all of the comparables (rental and expense).
   - ☐ Yes
   - ☐ No (Document):

4. Indicate Resources and Data utilized to research and verify information in the report under review:

5. Describe the analyses employed and any additional work required to complete the review.

6. Describe any extraordinary assumptions that were necessary to complete the review.

7. Is the appraisal/consulting work product under review complete, within the context of the requirements applicable to the assignment?
   - ☐ Yes
   - ☐ No (Document):

8. Is the data used in the development of the appraisal/consulting work product under review adequate and relevant to the assignment?
   - ☐ Yes
   - ☐ No (Document):

9. Are the adjustments made to the data presented, appropriate and supported?
   - ☐ Yes
   - ☐ No (Document):

10. Are the methods and techniques employed by the appraiser relevant to the assignment and

consistent with the appraiser's stated Scope of Work?

☐ Yes

☐ No (Document):

11. Are the appraiser's analyses, opinions and conclusions appropriate and reasonable?

☐ Yes

☐ No (Document):

B. Review of the Market Study: (Refer to Chapter 7.5 of the MAP Guide)

1. Does the Executive Summary comply with Section B.?

☐ Yes

☐ No (Document):

2. Is the description of the proposed project defined and characterized in compliance with Sections C?

☐ Yes

☐ No (Document):

3. Is the Housing Market Area (HMA) adequately defined in accordance with sections D?

☐ Yes

☐ No (Document):

4. Has the General Characteristics of the HMA been described in accordance with Section E?

☐ Yes

☐ No (Document):

5. Has the current market conditions been described in accordance with Section F.

☐ Yes

☐ No (Document):

6. Has there been an adequate discussion of Characteristics of Rental Units in the Pipeline - Under Construction and in Planning in accordance with Section G.

☐ Yes

☐ No (Document):

7. Does the market study include an estimate of future demand for the specified forecast period of _____ months? (typically 36 to 48 months)

☐ Yes

☐ No (Document)

8. Is the estimate of demand (#7 above) and the study supporting that estimate consistent with the guidelines contained within Section H?

☐ Yes

☐ No (Document)

9. For Age Restricted Projects - Were the technical and analytical methods used in the market study and all subsequent findings and conclusions consistent with the assumptions contained in Section I

☐ Yes

☐ No (Document):

☐ N/A

10. For Income Restricted Projects - Does the market study comply with the guidance contained in Section J and USPAP Advisory Opinion 14?

☐ Yes

☐ No (Document):

☐ N/A

11. Are the conclusions presented in the Market Study consistent with the facts presented; with the findings and recommendations based on a reasonable forecast of market supply/demand conditions and sound assumptions regarding capture rates, absorption, achievable rents, income affordability and similar factors?

☐ Yes

☐ No (Document):

12. Does Market Analysis assure that there is enough sustainable demand for additional units at the proposed rents without adversely impacting the existing supply of both HUD-insured and non HUD –insured projects?

C. HUD-92273 analysis:

1. One HUD-92273 analysis was completed by the Lender's appraiser for each unit breakdown?
   - ☐ Yes
   - ☐ No (Document)

2. A minimum of three appropriate and competitive comparables were used in each of the HUD-92273 analysis?
   - ☐ Yes
   - ☐ No (Document)

3 All amenities were identified and properly adjusted in the analysis?
   - ☐ Yes
   - ☐ No (Document)

4. Narrative explanations were given for amenity adjustments?
   - ☐ Yes
   - ☐ No

5. The HUD-92273 analysis completed by the Lender's appraiser conforms to the instructions listed in the MAP Guidebook?
   - ☐ Yes (Document)
   - ☐ No (Document)

D. HUD-92274 analysis:

1. A minimum of three market comparables were used in the HUD-92274 analysis?
   - ☐ Yes
   - ☐ No (Document)

2. The MAP Lender's appraiser used a HUD Insured project as an expense comparable?
   - ☐ Yes
   - ☐ No (Document)

3. The HUD Insured Project data was confirmed by the FASS or OPIIS System? (see MAP Guide 7.8.E.4)
   - ☐ Yes
   - ☐ No (Document)

4. The HUD-92274 analysis conforms to the instructions as stated in the MAP Guidebook?
   - ☐ Yes (Document)
   - ☐ No (Document)

E. The narrative explanation supporting the _____ % occupancy percentage estimated from the market for the project is:

- ☐ Acceptable
- ☐ Unacceptable (Document)

F. Pre-application Environmental Processing. The project's site is found acceptable, having no environmental or legal issues according to standards listed in the MAP Guidebook?

- ☐ Yes
- ☐ No (Document):

G. Other Technical Requirements:

1. The appraiser(s) and market analyst(s) employed by the lender met the qualifications and licensure requirements in accordance with Section 7.3 of the MAP Guide.
   - ☐ Yes
   - ☐ No (Document):

2. The appraiser complied with the Department's inspection requirements according to Section 7.6.A.15 of the MAP Guide.
   - ☐ Yes
   - ☐ No (Document):

H. From a review of appraisal/consulting exhibits the following conclusions are made:

1. The report reviewed supports the proposed rents and estimated rental income in compliance with the requirements found in Section 7.7 of the Guide: (Attach the rent schedule to this report.)

☐ Acceptable

☐ Unacceptable (Document)

2. The report reviewed supports the proposed total operating expenses in compliance with the requirements found in Section 7.8 of the Guide: (Attach the schedule of expenses to this report)

   $_____/unit Expense Ratio _____ % (of effective gross income)

   ☐ Acceptable

   ☐ Unacceptable (Document)

3. The report reviewed supports the Warranted Price of the Land of $_____ or the As Is Value of $ _____, as applicable, as noted on the lender's HUD-92264, in compliance with the requirements of Section 7.9 of the Guide.

   ☐ Yes

   ☐ No (Document)

4. For Section 220, 221(d)(3) or 221(d)(4) and 231 Substantial Rehabilitation, the "As Is" Value determination reconciled the values from these applicable approaches:

   Value by Cost Approach: _____

   Value By Sales Comparison Approach: _____

   Value by Income Approach: _____ Cap. % _____

   GIM or EGIM: _____

5. There has been an acceptable level of due diligence by the lender in the appraisal underwriting process as evidenced by the facts, analyses and conclusions presented in the underwriting summary and associated exhibits.

   ☐ Yes (Document)

   ☐ No (Document and prepare a referral to the Lender Quality Monitoring Division.)

Comments/Recommendations**:** (Attach additional pages as necessary.)

Review Appraiser's Certification:

I certify that, to the best of my knowledge and belief: The facts and data reported by the reviewer and used in the review process are true and correct.

1. The analysis, opinions, and conclusions in this review report are limited only by the assumptions and limiting conditions stated in this review report and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.

2. I have no present or prospective interest in the property that is the subject of this report and no personal interest with respect to the parties involved.

3. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.

4. My engagement in this assignment was not contingent upon developing or reporting predetermined results.

5. My compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in this review or from its use.

6. My analyses, opinions, and conclusions were developed and this review report was prepared in conformity with the Uniform Standards of Professional Appraisal Practice.

7. I did personally inspect the subject property of the work under review.

8. The following persons provided significant real, business, or personal property appraisal, appraisal review or consulting assistance to the person signing this certification:

HUD Appraiser's Signature_____Date_____

License Number/State_____

Team Leader: **____ Concurrence** **____ Non-concurrence**

Team Leader's Signature/Date_____Date_____

Reasons for Non-Concurrence: (Attach additional pages as necessary.)

HUD Appraiser Review

HUD Valuation Report - Technical Review of Multifamily Accelerated Processing – Firm Commitment Section 220, 221(d)(3), 221(d)(4) and 231

7B

This review of appraisal/consulting work product is to be completed in accordance with Standard 3 of the Uniform Standards of Professional Appraisal Practice (USPAP) currently in effect. The reviewer's client and intended user is the U. S. Department of Housing and Urban Development. The purpose of the review is to ascertain if the appraisal/consulting work product under review meets the applicable requirements of the USPAP and HUD, and that the work product has well-supported conclusions that can be used in making a recommendation to issue, or not issue a Firm Commitment for HUD mortgage insurance.

HUD Multifamily Hub: _____

Team Leader: _____

Reviewer: _____

Date Received for Review: _____ Pre-app. _____ Firm

Date of Pre-application Reviewer Site Visit: _____

Pre-application Review Report Completion Date:_____

Firm Review Report Completion Date: _____

SOA: _____ 220 _____ 221(d)(3) _____ 221(d)(4) _____ 231

Activity (check all that apply): ____ New Construction ____ Sub-rehab ____ Acquisition ____ Refinance

Project Name: _____

Case #: _____

Mortgagee: _____

Mortgagor: _____

Appraiser: _____

Market Analyst:_____

Date of Appraisal under Review: _____

Property and Ownership Interest Appraised: _____

Effective Date of Review: _____

A. Standard 3 Compliance:

1. The Reviewer was able to adequately identify the property that is the subject of this review.
   - ☐ Yes
   - ☐ No (Document)

2. If applicable, the Reviewer has re- inspected the exterior of the subject and the following units (if applicable, list)
   - ☐ Yes
   - ☐ No (Document)
   - ☐ Not Applicable

3. If applicable, the Reviewer has re-inspected the exterior of all of the original comparables and/or inspected any new comparables (rental and expense).
   - ☐ Yes
   - ☐ No (Document)
   - ☐ Not Applicable

4. Indicate Resources and Data utilized to research and verify information in the report under review:

5. Describe the analyses employed and any additional work required to complete the review:

6. Describe any extraordinary assumptions that were necessary to complete the review:

7. Is the appraisal/consulting work product under review complete, within the context of the requirements applicable to the assignment?
   - ☐ Yes
   - ☐ No (Document):

8. Is the data used in the development of the appraisal/consulting work product under review adequate and relevant to the assignment?
   - ☐ Yes

☐ No (Document):

9. Are the adjustments made to the data presented, appropriate and supported?

☐ Yes

☐ No (Document):

10. Are the methods and techniques employed by the appraiser relevant to the assignment and consistent with the appraiser's stated Scope of Work?

☐ Yes

☐ No (Document):

11. Are the appraiser's analyses, opinions and conclusions appropriate and reasonable

☐ Yes

☐ No (Document):

B. Review of additional Market Study submissions since Pre-application: (Refer to Section 7.5 of the MAP Guide)

1. Was there any new information submitted to update the Market Study that was reviewed at Pre-application?

☐ Yes

☐ No

2. Is the new information consistent with the facts presented; with the findings and recommendations based on a reasonable forecast of market supply/demand conditions and sound assumptions regarding capture rates, absorption, achievable rents, income affordability and similar factors? (Section H)

☐ Yes

☐ No (Document)

☐ Not Applicable

3. Does the updated Market Analysis assure that there is enough sustainable demand for additional units at the proposed rents without adversely impacting the existing supply of both HUD-insured and non HUD-insured projects?

   ☐ Yes

   ☐ No (Document)

   ☐ Not Applicable

C. HUD-92273 analysis, if different from Pre-application

1. One HUD-92273 analysis was completed by the Lender's appraiser for each unit breakdown, a minimum of three appropriate and competitive comparables were used in each of the HUD-92273 analysis and analysis completed by the Lender's appraiser conforms to the instructions listed in the MAP Guidebook?

   ☐ Yes

   ☐ No (Document)

   ☐ Not Applicable

2. All amenities were identified and properly adjusted in the analysis?

   ☐ Yes

   ☐ No (Document)

   ☐ Not Applicable

3. Narrative explanations were given for amenity adjustments?

   ☐ Yes

   ☐ No (Document)

   ☐ Not Applicable

D. **HUD-92274 analysis, if different from Pre-application**:

1. A minimum of three market comparables were used in the HUD-92274 analysis, and the analysis conforms to the instructions as stated in the MAP Guidebook.?

   ☐ Yes

   ☐ No (Document)

   ☐ Not Applicable

2. The MAP Lender's appraiser used a HUD Insured project as an expense comparable?

   ☐ Yes

☐ No (Document)

☐ Not Applicable

3. The HUD Insured Project data was confirmed by the FASS or OPIIS System? (see MAP Guide 7.8.E.4)

☐ Yes

☐ No (Document)

☐ Not Applicable

E. The narrative explanation supporting the _____ % occupancy percentage estimated from the market for the project is:

☐ Acceptable

☐ Unacceptable (Document)

F. Environmental Processing:

1. The lender's Phase I Environmental Report, Phase II Report, if applicable, and any additional studies, as noted below, have been reviewed and are consistent with the conclusions contained on the completed HUD-4128.

☐ Yes

☐ No (Document)

2. The subject meets the Department's Environmental requirements in accordance with Chapter 9 of the MAP Guide:

☐ Yes

☐ No (Document):

3. All third party environmental reports identify the U.S. Department of Housing and Urban Development as an authorized user of the report:

☐ Yes

☐ No (Document):

G. HUD-92264 Analysis:

1. A HUD-92264 was properly completed and signed by the underwriter.

☐ Yes

☐ No (Document):

2. The analyses and conclusions contained in the HUD-92264 are consistent with the narrative report and all other supporting forms and documents

   ☐ Yes

   ☐ No (Document):

H. Other Technical Requirements:

1. The appraiser(s) and market analyst(s) employed by the lender met the qualifications and licensure requirements in accordance with Section 7.3 of the MAP Guide.

   ☐ Yes

   ☐ No (Document):

2. The appraiser complied with the Department's inspection requirements according to Section 7.6.A.15 of the MAP Guide.

   ☐ Yes

   ☐ No (Document):

3. A HUD-92264-T, as appropriate, is completed (if required), according to Section 7.17 of the MAP Guide

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

4. For Subjects that have LIHTCs or Section 8 project based subsidies; the appraiser <u>has not</u> attributed any benefit for the LIHTC award or Section 8 subsidies in the estimate of Warranted Price of Land in new construction or the As Is value in substantial rehabilitation cases. (A "Yes" response means that no benefit was attributed.)

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

5. The Operating Deficit estimate of $ _____ covering a period of _____ months as entered on the lender's HUD-92264 form was properly calculated in accordance with the requirements in Section 7.14 of the Guide. (Note: If an Operating Deficit Escrow is not being required, there must be adequate documentation to support that the escrow is not needed.)

☐ Yes

☐ No (Document):

☐ Not Required (Document):

6. The lender's HUD-92264-A shows that there is a Tax Abatement that increases the Net Operating Income by $ _____. This amount has been properly calculated according to the requirements in Section 7.16 of the Guide.

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

7. The market analysis portion of the self-contained appraisal complies with the relevant guidance contained in Section 7.6.A.17 of the Guide.

   ☐ Yes

   ☐ No (Document):

I. From a review of appraisal/consulting exhibits the following conclusions are made:

1. The report reviewed supports the proposed rents and estimated rental income in compliance with the requirements found in Section 7.7 of the Guide: (Attach the rent schedule to this report.)

   ☐ Yes

   ☐ No (Document)

2. The report reviewed supports the proposed total operating expenses in compliance with the requirements found in Section 7.8 of the Guide: (Attach the schedule of expenses to this report)

   $_____/unit Expense Ratio _____ % (of effective gross)

   ☐ Yes

   ☐ No (Document)

3. The resulting Net Operating Income is: $ _____.

4. The report reviewed supports the Warranted Price of the Land of $_____ or the As Is Value of $ _____, as applicable, as noted on the lender's HUD-92264, in compliance with the requirements of Sections 7.9 and 7.13 of the Guide.

   ☐ Yes

☐ No (Document)

5. For Section 220, 221(d)(3) or 221(d)(4) Substantial Rehabilitation, the As Is Value determination reconciled the values from these applicable approaches:

   Value by Cost Approach: _____

   Value By Sales Comparison Approach: _____

   Value by Income Approach: _____ Cap. % _____

   GIM or EGIM: _____

6. The Total Replacement Cost of the project as shown in Section G on the lender's

   HUD-92264 is $_____. Section G has been properly completed and is consistent with the lender submitted replacement cost by formula.

   ☐ Yes

   ☐ No (Document)

7. The report reviewed contains thorough documentation supporting the Remaining Economic Life Estimate of _____ years, in accordance with the requirements of Section 7.4. of the MAP Guide.

   ☐ Yes

   ☐ No (Document)

8. The Trial HUD-92264-A submitted by the lender was properly completed and indicates a

   Criterion # _____ limited mortgage of $ _____.

   ☐ Yes

   ☐ No (Document)

9. For Substantial Rehabilitation of Section 231**,** the report reviewed indicates an

   As Is Value of $ _____, reconciled from the values of these applicable approaches;

   Value by Cost Approach: _____

   Value By Sales Comparison Approach: _____

Value by Income Approach: _____ Cap. % _____,

GIM or EGIM _____ and the **Value After Rehabilitation of** $ _____,

reconciled from the values of these applicable approaches;

Value by Cost Approach: _____

Value By Sales Comparison Approach: _____

Value by Income Approach: _____ Cap. % _____,

GIM or EGIM _____as noted on the lender's HUD-92264.

If applicable, a Residual "as is" Value by formula was completed yielding an "as is" value of $ _____.

The Total Replacement Cost of the Project (Section G, Line 74 of the form HUD 92264) is: $ _____.

10. The reconciliation provides an adequate discussion relating to the quality and quantity of the information presented in the applicable approaches to value and the final value estimated is credible and can be relied upon to make underwriting decisions:

    ☐ Yes

    ☐ No (Document)

11. There has been an acceptable level of due diligence by the lender in the appraisal underwriting process as evidenced by the facts, analyses and conclusions presented in the underwriting summary and associated exhibits.

    ☐ Yes (Document)

    ☐ No (Document and prepare a referral to the Lender Quality Monitoring Division.)

Comments/Recommendations: (Attach additional pages as necessary.)

Review Appraiser's Certification:

I certify that, to the best of my knowledge and belief:

1. The facts and data reported by the reviewer and used in the review process are true and correct.
2. The analysis, opinions, and conclusions in this review report are limited only by the

assumptions and limiting conditions stated in this review report and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.

3. I have no present or prospective interest in the property that is the subject of this report and no personal interest with respect to the parties involved.
4. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
5. My engagement in this assignment was not contingent upon developing or reporting predetermined results.
6. My compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in this review or from its use.
7. My analyses, opinions, and conclusions were developed and this review report was prepared in conformity with the Uniform Standards of Professional Appraisal Practice.
8. I did personally inspect the subject property of the work under review.
9. The following persons provided significant real, business, or personal property appraisal, appraisal review or consulting assistance to the person signing this certification:

HUD Appraiser's Signature_____Date_____

License Number/State_____

Team Leader: **____ Concurrence** **____ Non-concurrence**:

Team Leader's Signature/Date_____Date_____

Reasons for Non-concurrence: (Attach additional pages as necessary)

HUD Appraiser Review

HUD Valuation Report - Technical Review of Multifamily Accelerated Processing – Direct to Firm Commitment Section 220, 221(d)(3), 221(d)(4) and 231

7C

This review of appraisal/consulting work product is to be completed in accordance with Standard 3 of the Uniform Standards of Professional Appraisal Practice (USPAP) currently in effect. The reviewer's client and intended user is the U. S. Department of Housing and Urban Development. The purpose of the review is to ascertain if the appraisal/consulting work product under review meets the applicable requirements of the USPAP and HUD, and that the work product has well-supported conclusions that can be used in making a recommendation to issue, or not issue a Firm Commitment for HUD mortgage insurance.

HUD Multifamily Hub: _____

Team Leader: _____

Reviewer: _____

Date Received for Review: _____

Date of Reviewer Site Visit: _____

Review Report Completion Date: _____

SOA: _____ 220 _____ 221(d)(3) _____ 221(d)(4) _____ 231

Activity: (check all that apply) ____ New Construction ____ Sub-rehab ____ Acquisition ____ Refinance

Project Name: _____

Case #: _____

Mortgagee: _____

Mortgagor: _____

Appraiser: _____

Market Analyst:_____

Date of Appraisal under Review: _____

Property and Ownership Interest Appraised: _____

Effective Date of Review: _____

A. Standard 3 Compliance:

1. The Reviewer was able to adequately identify the property that is the subject of this review.
   - ☐ Yes
   - ☐ No (Document)

2. The Reviewer inspected the exterior of the subject and the following units (if applicable, list)
   - ☐ Yes
   - ☐ No (Document)

3. The Reviewer inspected the exterior of all of the comparables (rental and expense).
   - ☐ Yes
   - ☐ No (Document):

4. Indicate Resources and Data utilized to research and verify information in the report under review:

6. Describe the analyses employed and any additional work required to complete the review:

7. Describe any extraordinary assumptions that were necessary to complete the review:

8. Is the appraisal/consulting work product under review complete, within the context of the requirements applicable to the assignment?
   - ☐ Yes
   - ☐ No (Document):

9. Is the data used in the development of the appraisal/consulting work product under review adequate and relevant to the assignment?
   - ☐ Yes
   - ☐ No (Document):

10. Are the adjustments made to the data presented, appropriate and supported?
    - ☐ Yes
    - ☐ No (Document):

11. Are the methods and techniques employed by the appraiser relevant to the assignment and consistent with the appraiser's stated Scope of Work?
    - ☐ Yes
    - ☐ No (Document):

12. Are the appraiser's analyses, opinions and conclusions appropriate and reasonable
    - ☐ Yes
    - ☐ No (Document):

B. Review of the Market Study: (Refer to Chapter 7.5 of the MAP Guide)

1. Does the Executive Summary comply with Section B.?
    - ☐ Yes
    - ☐ No (Document):

2. Is the description of the proposed project defined and characterized in compliance with Sections C?
    - ☐ Yes
    - ☐ No (Document):

3. Is the Housing Market Area (HMA) adequately defined in accordance with sections D?
    - ☐ Yes
    - ☐ No (Document):

4. Has the General Characteristics of the HMA been described in accordance with Section E?
    - ☐ Yes
    - ☐ No (Document):

5. Has the current market conditions been described in accordance with Section F.
   - ☐ Yes
   - ☐ No (Document):

6. Has there been an adequate discussion of Characteristics of Rental Units in the Pipeline - Under Construction and in Planning in accordance with Section G.
   - ☐ Yes
   - ☐ No (Document):

7. Does the market study include an estimate of future demand for the specified forecast period of _____ months? (typically 36 to 48 months)
   - ☐ Yes
   - ☐ No (Document)

8. Is the estimate of demand (#7 above) and the study supporting that estimate consistent with the guidelines contained within Section H?
   - ☐ Yes
   - ☐ No (Document)

9. For Age Restricted Projects - Were the technical and analytical methods used in the market study and all subsequent findings and conclusions consistent with the assumptions contained in Section I
   - ☐ Yes
   - ☐ No (Document):
   - ☐ N/A

10. For Income Restricted Projects - Does the market study comply with the guidance contained in Section J and USPAP Advisory Opinion 14?
    - ☐ Yes
    - ☐ No (Document):
    - ☐ N/A

11. Are the conclusions presented in the Market Study consistent with the facts presented; with the findings and recommendations based on a reasonable forecast of market supply/demand

conditions and sound assumptions regarding capture rates, absorption, achievable rents, income affordability and similar factors?

☐ Yes

☐ No (Document):

12. Does Market Analysis assure that there is enough sustainable demand for additional units at the proposed rents without adversely impacting the existing supply of both HUD-insured and non HUD –insured projects?

C. HUD-92273 analysis:

1. One HUD-92273 analyses was completed by the Lender's appraiser for each unit breakdown?

   ☐ Yes

   ☐ No (Document)

2. A minimum of three appropriate and competitive comparables were used in each of the HUD- 92273 analysis?

   ☐ Yes

   ☐ No (Document)

3. All amenities were identified and properly adjusted in the analysis?

   ☐ Yes

   ☐ No (Document)

4. Narrative explanations were given for amenity adjustments?

   ☐ Yes

   ☐ No

5. The HUD-92273 analysis completed by the Lender's appraiser conforms to the instructions listed in the MAP Guidebook?

   ☐ Yes (Document)

   ☐ No (Document)

D. HUD-92274 Analysis:

1. A minimum of three market comparables were used in the HUD-92274 analysis?
   - ☐ Yes
   - ☐ No (Document)

2. The MAP Lender's appraiser used a HUD Insured project as an expense comparable?
   - ☐ Yes
   - ☐ No (Document)

3. The HUD Insured Project data was confirmed by the FASS or OPIS Systems? (see MAP Guide 7.7.)
   - ☐ Yes
   - ☐ No (Document)

4. The HUD-92274 analysis conforms to the instructions as stated in the MAP Guidebook?
   - ☐ Yes (Document)
   - ☐ No (Document)

5. The narrative explanation supporting the _____ % occupancy percentage estimated from the market for the project is:
   - ☐ Acceptable
   - ☐ Unacceptable (Document)

F. Environmental Processing:

1. The lender's Phase I Environmental Report, Phase II Report, if applicable, and any additional studies, as noted below, have been reviewed and are consistent with the conclusions contained on the completed HUD-4128.
   - ☐ Yes
   - ☐ No (Document)

2. The subject meets the Department's Environmental requirements in accordance with Chapter 9 of the MAP Guide:
   - ☐ Yes
   - ☐ No (Document):

3. All third party environmental reports identify the U.S. Department of Housing and Urban Development as an authorized user of the report:
   - ☐ Yes
   - ☐ No (Document):

G. HUD-92264 Analysis:

1. A HUD-92264 was properly completed and signed by the underwriter.
   - ☐ Yes
   - ☐ No (Document):

2. The analyses and conclusions contained in the HUD-92264 are consistent with the narrative report and all other supporting forms and documents.
   - ☐ Yes
   - ☐ No (Document):

H. Other Technical Requirements:

1. The appraiser(s) and market analyst(s) employed by the lender met the qualifications and licensure requirements in accordance with Section 7.3 of the MAP Guide.
   - ☐ Yes
   - ☐ No (Document):

2. The appraiser complied with the Department's inspection requirements according to Section 7.4.of the MAP Guide.
   - ☐ Yes
   - ☐ No (Document):

3. A HUD-92264-T, as appropriate, were completed (if required) according to Chapter 7 of the Guide and HN 92-97.

☐ N/A

☐ Yes

☐ No (Document):

4. For Subjects that have LIHTC's or Section 8 project based subsidies; the appraiser has not attributed any benefit for the LIHTC award or Section 8 subsidies in the estimate of Warranted Price of Land in new construction or the As Is value in substantial rehabilitation cases. (A "Yes" response means that no benefit was attributed.)

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

5. The Operating Deficit estimate of $ _____ covering a period of _____ months as entered on the lender's HUD-92264 form was properly calculated in accordance with the requirements in Section 7.14 of the Guide. (Note: If an Operating Deficit Escrow is not being required, there must be adequate documentation to support that the escrow is not needed.)

   ☐ Yes

   ☐ No (Document):

   ☐ Not Required (Document):

6. The lender's HUD-92264-A shows that there is a Tax Abatement that increases the Net Operating Income by $ _____. This amount has been properly calculated according to the requirements in Section 7.17 of the Guide.

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

7. The market analysis portion of the self-contained appraisal complies with the relevant guidance contained in Section 7.6.A.17 of the Guide.

   ☐ Yes

   ☐ No (Document):

I. From a review of appraisal/consulting exhibits the following conclusions are made:

1. The report reviewed supports the proposed rents and estimated rental income in compliance with the requirements found in Section 7.6 of the Guide: (Attach the rent schedule to this report.)

   ☐ Yes

   ☐ No (Document)

2. The report reviewed supports the proposed total operating expenses in compliance with the requirements found in Section 7.7 of the Guide: (Attach the schedule of expenses to this report)
   $_____/unit Expense Ratio _____ % (of effective gross)
   ☐ Yes
   ☐ No (Document)

J. The resulting Net Operating Income is: $ _____.

K. The report reviewed supports the Warranted Price of the Land of $_____

or the As Is Value of $ _____, as applicable, as noted on the lender's HUD-92264, in compliance with the requirements of Section 7.8 of the Guide.

☐ Yes

☐ No (Document)

L. For Section 220, 221(d)(3) or 221(d)(4) Substantial Rehabilitation:

1. The As Is Value determination reconciled the values from these applicable approaches:
   Value by Cost Approach: _____
   Value By Sales Comparison Approach: _____
   Value by Income Approach: _____ Cap. % _____
   GIM or EGIM: _____

2. The Total Replacement Cost of the project as shown in Section G on the Lender's HUD-92264 is $_____. Section G has been properly completed and is consistent with the lender submitted replacement cost by formula.
   ☐ Yes
   ☐ No (Document)

3. The report reviewed contains thorough documentation supporting the Remaining Economic Life Estimate of _____ years, in accordance with the requirements of Section 7.4 of the Guide.
   ☐ Yes
   ☐ No (Document)

4. The Trial HUD-92264-A submitted by the lender was properly completed and indicates a Criterion # _____ limited mortgage of $ _____.

   ☐ Yes
   ☐ No (Document)

5. For a Substantial Rehabilitation of Section 231, the report reviewed indicates an **As Is Value of** $ _____, reconciled from the values of these applicable approaches;

   Value by Cost Approach: _____

   Value By Sales Comparison Approach: _____

   Value by Income Approach: _____ Cap. % _____,

   GIM or EGIM _____

   and the **Value After Rehabilitation of** $ _____, reconciled from the values of these applicable approaches;

   Value by Cost Approach: _____

   Value By Sales Comparison Approach: _____

   Value by Income Approach: _____ Cap. % _____,

   GIM or EGIM _____ as

   noted on the lender's HUD-92264.

   If applicable, a Residual "as is" Value by formula was completed yielding an "as is" value of $ _____.

   The Total Replacement Cost of the Project (Section G, Line 74 of the form HUD 92264) is: $ _____.

6. The reconciliation provides an adequate discussion relating to the quality and quantity of the information presented in the applicable approaches to value and the final value estimated is credible and can be relied upon to make underwriting decisions:

   ☐ Yes
   ☐ No (Document)

7. There has been an acceptable level of due diligence by the lender in the appraisal underwriting process as evidenced by the facts, analyses and conclusions presented in the underwriting summary and associated exhibits.

   ☐ Yes (Document)

   ☐ No (Document and prepare a referral to the Lender Quality Monitoring Division.)

Comments/Recommendations: (Attach additional pages as necessary.)

Review Appraiser's Certification:

I certify that, to the best of my knowledge and belief:

1. The facts and data reported by the reviewer and used in the review process are true and correct.
2. The analysis, opinions, and conclusions in this review report are limited only by the assumptions and limiting conditions stated in this review report and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.
3. I have no present or prospective interest in the property that is the subject of this report and no personal interest with respect to the parties involved.
4. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
5. My engagement in this assignment was not contingent upon developing or reporting predetermined results.
6. My compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in this review or from its use.
7. My analyses, opinions, and conclusions were developed and this review report was prepared in conformity with the Uniform Standards of Professional Appraisal Practice.
8. I did personally inspect the subject property of the work under review.
9. The following persons provided significant real, business, or personal property appraisal, appraisal review or consulting assistance to the person signing this certification:

HUD Appraiser's Signature_____Date_____

License Number/State_____

Team Leader: ____ **Concurrence** ____ **Non-concurrence**:

Team Leader's Signature/Date_____Date_____

Reasons for Non-concurrence: (Attach additional pages as necessary)

HUD Appraiser Review

HUD Valuation Report - Technical Review of Multifamily Accelerated Processing – Firm Commitment Section 223(f)

7D

This review of appraisal/consulting work product is to be completed in accordance with Standard 3 of the Uniform Standards of Professional Appraisal Practice (USPAP) currently in effect. The reviewer's client and intended user is the U. S. Department of Housing and Urban Development. The purpose of the review is to ascertain if the appraisal/consulting work product under review meets the applicable requirements of the USPAP and HUD, and that the work product has well-supported conclusions that can be used in making a recommendation to issue, or not issue a Firm Commitment for HUD mortgage insurance. NOTE: If Applicable the HUD Review Appraiser will complete a review of the separate market study in format contained at the end of this Appendix.

HUD Multifamily Hub: _____

Team Leader: _____

Reviewer: _____

Date Received for Review: _____

Date of Reviewer Site Visit: _____

Review Report Completion Date: _____

Activity: (check all that apply) _____ Acquisition _____ Refinance

Project Name: _____

Case #: _____

Mortgagee: _____

Mortgagor: _____

Appraiser: _____

Date of Appraisal under Review: _____

Ownership Interest Appraised: _____

Effective Date of Review: _____

A. Standard 3 Compliance:

1. The Reviewer was able to adequately identify the property that is the subject of this review.
   - ☐ Yes
   - ☐ No (Document)

2. The Reviewer inspected the exterior of the subject and the following units (if applicable, list)
   - ☐ Yes
   - ☐ No (Document)

3. The Reviewer inspected the exterior of all of the comparables (rental and expense).
   - ☐ Yes
   - ☐ No (Document):

4 Indicate Resources and Data utilized to research and verify information in the report under review:

5. Describe the analyses employed and any additional work required to complete the review:

6. Describe any extraordinary assumptions that were necessary to complete the review:
7. Is the appraisal/consulting work product under review complete, within the context of the requirements applicable to the assignment?
   - ☐ Yes
   - ☐ No (Document):

8. Is the data used in the development of the appraisal/consulting work product under review adequate and relevant to the assignment?
   - ☐ Yes
   - ☐ No (Document):

9. Are the adjustments made to the data presented, appropriate and supported?
   - ☐ Yes
   - ☐ No (Document):

10. Are the methods and techniques employed by the appraiser relevant to the assignment and consistent with the appraiser's stated Scope of Work?
    - ☐ Yes
    - ☐ No (Document):

11. Are the appraiser's analyses, opinions and conclusions appropriate and reasonable
    - ☐ Yes
    - ☐ No (Document):

B. Review of the Appraiser's Analysis of the Current Market for the Subject:

1. Is the Market Area specifically defined and characterized?
   - ☐ Yes
   - ☐ No (Document):

2. Is there adequate discussion of Current Market Conditions including projects under construction and in planning?
   - ☐ Yes
   - ☐ No (Document):

3 (For Age Restricted Projects). Has this sub-market been adequately defined and characterized?

☐ Yes

☐ No (Document):

☐ N/A

4. Are the conclusions presented in the Appraiser's Market Analysis consistent with the facts presented; with the findings and recommendations based on a reasonable forecast of market supply/demand conditions and sound assumptions regarding capture rates, absorption, achievable rents, income affordability and similar factors?

   ☐ Yes

   ☐ No (Document):

5. Does Market Analysis assure that there is enough sustainable demand for the long term use of the property as an apartment project?

   ☐ Yes

   ☐ No (Document):

C. HUD-92273 analysis:

1. One HUD-92273 analysis was completed by the Lender's appraiser for each unit breakdown?

   ☐ Yes

   ☐ No (Document)

2. A minimum of three appropriate and competitive comparables were used in each of the HUD- 92273 analysis?

   ☐ Yes

   ☐ No (Document)

3. All amenities were identified and properly adjusted in the analysis?

   ☐ Yes

   ☐ No (Document)

4. Narrative explanations were given for amenity adjustments?

   ☐ Yes

   ☐ No

5. The HUD-92273 analysis completed by the Lender's appraiser conforms to the instructions

listed in the MAP Guidebook?

☐ Yes (Document)

☐ No (Document)

D. HUD-92274 analysis:

1. A minimum of three market comparables were used in the HUD-92274 analysis?

☐ Yes

☐ No (Document)

2. The MAP Lender's appraiser used a HUD Insured project as an expense comparable?

☐ Yes

☐ No (Document)

3. The HUD Insured Project data was confirmed by the FASS System? (see MAP Guide Chapter7)

☐ Yes

☐ No (Document)

4. The HUD-92274 analysis conforms to the instructions as stated in the MAP Guidebook?

☐ Yes (Document)

☐ No (Document)

E. The narrative explanation supporting the _____ % occupancy percentage estimated from the market for the project is:

☐ Acceptable

☐ Unacceptable (Document)

F. Environmental Processing:

1. The lender's Phase I Environmental Report, Phase II Report, if applicable, and any additional studies, as noted below, have been reviewed and are consistent with the conclusions contained on the completed HUD-4128.

☐ Yes

☐ No (Document)

2. The subject meets the Department's Environmental requirements in accordance with

Chapter 9 of the MAP Guide:

☐ Yes
☐ No (Document):

3. All third party environmental reports identify the U.S. Department of Housing and Urban Development as an authorized user of the report:
   ☐ Yes
   ☐ No (Document):

G. HUD-92264 Analysis:

1 A HUD-92264 was properly completed and signed by the underwriter.
   ☐ Yes
   ☐ No (Document):

2. The analyses and conclusions contained in the HUD-92264 are consistent with the narrative report and all other supporting forms and documents
   ☐ Yes
   ☐ No (Document):

H. Other Technical Requirements:

1. The appraiser(s) and market analyst(s) employed by the lender met the qualifications and licensure requirements in accordance with Section 7.3 of the MAP Guide.
   ☐ Yes
   ☐ No (Document):
2. The appraiser complied with the Department's inspection requirements according to Section 7.4. of the MAP Guide.
   ☐ Yes
   ☐ No (Document):

3. A HUD-92264-T and Subsidy Layering Review, as appropriate, were completed as required according to Chapter 7 and HN 92-97.
   ☐ N/A

☐ Yes

☐ No (Document):

4. For Subjects that have LIHTCs or Section 8 project based subsidies; the appraiser has not attributed any benefit for the LIHTC award or Section 8 subsidies in the estimate of Warranted Price of Land in new construction or the As Is value in substantial rehabilitation cases. (A "Yes" response means that no benefit was attributed.)

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

5. The Operating Deficit estimate of $ _____ covering a period of _____ months as entered on the lender's HUD-92264 form was properly calculated in accordance with the requirements in Section 7.14 of the Guide. (Note: If an Operating Deficit Escrow is not being required, there must be adequate documentation to support that the escrow is not needed.)

   ☐ Yes

   ☐ No (Document):

   ☐ Not Required (Document):

6. The lender's HUD-92264-A shows that there is a Tax Abatement that increases the Net Operating Income by $ _____. This amount has been properly calculated according to the requirements in Section 7.17 of the Guide.

   ☐ N/A

   ☐ Yes

   ☐ No (Document):

7. The market analysis portion of the self-contained appraisal complies with the relevant guidance contained in Section 7.6.A.17 of the Guide.

   ☐ Yes

   ☐ No (Document):

I. From a review of appraisal/consulting exhibits the following conclusions are made:

1. The report reviewed supports the proposed rents and estimated rental income in compliance with the requirements found in Section 7.6 of the Guide: (Attach the rent schedule to this report.)

☐ Yes

☐ No (Document)

2. The report reviewed supports the proposed total operating expenses in compliance with the requirements found in Sections 7.4 and 7.7 of the Guide: (Attach the schedule of expenses to this report)

   $_____/unit Expense Ratio _____ % (of effective gross)

   ☐ Yes

   ☐ No (Document)

3. The resulting Net Operating Income is: $ _____.

4. The report reviewed supports the Warranted Price of the Land of $_____or the As Is Value of $ _____, as applicable, as noted on the lender's HUD-92264, in compliance with the requirements of Section 7.8 of the Guide.

   ☐ Yes

   ☐ No (Document)

5. The Total Replacement Cost of the project as shown in Section G on the lenders HUD-92264 is $_____. Section G has been properly completed and is consistent with the lender submitted replacement cost by formula.

   ☐ Yes

   ☐ No (Document)

6. The reconciliation of the applicable approaches and final value determination for the subject is summarized as follows:

   Value by Cost Approach: _____

   Value By Sales Comparison Approach: _____

   Value by Income Approach:_____ Cap. % _____

   GIM or EGIM _____ Value Estimate: _____

7. The reconciliation provides an adequate discussion relating to the quality and quantity of the information presented in the applicable approaches to value and the final value estimated is credible and can be relied upon to make underwriting decisions:

   ☐ Yes

   ☐ No (Document)

8. The report reviewed contains thorough documentation supporting the Remaining Economic Life Estimate of _____ years, in accordance with the requirements of Section 7.4 of the Guide.

   ☐ Yes

   ☐ No (Document)

9. The Trial HUD-92264-A submitted by the lender was properly completed and indicates a Criterion # _____ limited mortgage of $ _____.

   ☐ Yes

   ☐ No (Document)

10. There has been an acceptable level of due diligence by the lender in the appraisal underwriting process as evidenced by the facts, analyses and conclusions presented in the underwriting summary and associated exhibits.

    ☐ Yes (Document)

    ☐ No (Document and prepare a referral to the Lender Qualification Monitoring Division.)

Comments/Recommendations: (Attach additional pages as necessary.)

Review Appraiser's Certification:

I certify that, to the best of my knowledge and belief:

1. The facts and data reported by the reviewer and used in the review process are true and correct.
2. The analysis, opinions, and conclusions in this review report are limited only by the assumptions and limiting conditions stated in this review report and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.
3. I have no present or prospective interest in the property that is the subject of this report and no personal interest with respect to the parties involved.
4. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
5. My engagement in this assignment was not contingent upon developing or reporting predetermined results.
6. My compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in this review or from its use.
7. My analyses, opinions, and conclusions were developed and this review report was prepared in conformity with the Uniform Standards of Professional Appraisal Practice.
8. I did personally inspect the subject property of the work under review.
9. The following persons provided significant real, business, or personal property appraisal, appraisal review or consulting assistance to the person signing this certification:

HUD Appraiser's Signature_____Date_____

License Number/State_____

Team Leader: ____ **Concurrence** ____ **Non-concurrence**:

Team Leader's Signature/Date_____Date_____

Reasons for Non-concurrence: (Attach additional pages as necessary)

If Applicable the HUD Review Appraiser will complete the following review of the separate market study.

Review of the Market Study: (Refer to Chapter 7.5 of the MAP Guide)

5. Does the Executive Summary comply with Section B.?

   ☐ Yes

   ☐ No (Document):

10. Is the description of the proposed project defined and characterized in compliance with Sections C?

    ☐ Yes

    ☐ No (Document):

11. Is the Housing Market Area (HMA) adequately defined in accordance with sections D?

    ☐ Yes

    ☐ No (Document):

12. Has the General Characteristics of the HMA been described in accordance with Section E?

    ☐ Yes

    ☐ No (Document):

13. Has the current market conditions been described in accordance with Section F.

    ☐ Yes

    ☐ No (Document):

14. Has there been an adequate discussion of Characteristics of Rental Units in the Pipeline - Under Construction and in Planning in accordance with Section G.

    ☐ Yes

    ☐ No (Document):

15. Does the market study include an estimate of future demand for the specified forecast period of _____ months? (typically 36 to 48 months)

    ☐ Yes

☐ No (Document)

16. Is the estimate of demand (#7 above) and the study supporting that estimate consistent with the guidelines contained within Section H?

☐ Yes

☐ No (Document)

17. For Age Restricted Projects - Were the technical and analytical methods used in the market study and all subsequent findings and conclusions consistent with the assumptions contained in Section I

☐ Yes

☐ No (Document):

☐ N/A

13. For Income Restricted Projects - Does the market study comply with the guidance contained in Section J and USPAP Advisory Opinion 14?

☐ Yes

☐ No (Document):

☐ N/A

14. Are the conclusions presented in the Market Study consistent with the facts presented; with the findings and recommendations based on a reasonable forecast of market supply/demand conditions and sound assumptions regarding capture rates, absorption, achievable rents, income affordability and similar factors?

☐ Yes

☐ No (Document):

15. Does Market Analysis assure that there is enough sustainable demand for additional units at the proposed rents without adversely impacting the existing supply of both HUD-insured and non HUD –insured projects?

Appendix 8

Mortgage Credit Underwriting and Processing Requirements

Table of Contents

	Title
8A	HUD Mortgage Credit Review of Lender's Underwriter's Processing
8B	Payoff Letter for Existing Mortgage
8C	How to Analyze Financial Statements

HUD Mortgage Credit Review of Lender's Underwriter's Processing

8A

HUD Office Name _____

Application Submission Date _____

Project Name _____

Project Location (City, State) _____

MAP Lender Name _____

Mortgagor Name _____

☐ Pre-Applications ☐ Firm Commitment Application

A. Pre-Application

1. Review of Lender's Underwriter's estimate of the replacement cost:

   If unacceptable, state reasons:

2. Review of Lender's Underwriter's estimate of the insurance mortgage amount:

   If unacceptable, indicate reasons:

3. Acceptability of any nonprofit sponsors/mortgagors:

   If unacceptable, indicate reasons:

B. Firm Commitment.

1. HUD programs previous participation (HUD-2530) reviews:

   Listing of unacceptable principals:

2. General review of the Lender's Underwriter's report and the HUD Form-2264-A, comments:

If report unacceptable, state reasons:

3. Acceptability of the sponsor, mortgagor and its key principals, and the contractor:

   If unacceptable, state reasons:

4. Acceptability of the maximum mortgage amount:

   If unacceptable, state reasons:

5. Acceptability of the financial requirements for settlement:

   If unacceptable, state reasons:

6. Verifications of sources of funds to meet cash requirements:

I have reviewed the subject project and hereby make the following recommendations(s):

Reviewer:
Name of Reviewer: _____
Signature and Date of Review _____ Date _____
Concurrence:
Name of Team Leader _____
Signature and Date of Concurrence _____ Date _____

Payoff Letter for Existing Mortgage

8B

Name and Address Bank:

Madam/ Sir:

Subject:

Name and Address of Project:

Borrower's Account No. _____

This office has received an application for FHA mortgage insurance for the subject project. We are advised that your firm is the mortgagee. Please provide us with the following information:

Date of Mortgage _____

Original Amount $_____ Monthly Payment Amount $_____

Next Payment Due $_____

Present Mortgage Balance $_____ As of (Date) _____

Other Amounts Due: Interest $_____ Penalties $_____

Total Payoff Balance (Excluding Forgiven Indebtedness, Rebates, etc.) $_____

Balance of Escrow, Reserves, etc. (Itemize) $_____
$_____ $_____

Is Debt Current: Yes ____ No _____ Satisfactory _____ Unsatisfactory _____

Other known Indebtedness against property (explain)_____

_____

Remarks _____

_____

Date _____ Signature _____

Title _____

Information provided will be used solely for our evaluation and will otherwise be held in confidence. We are enclosing a stamped, self-addressed envelope. Please replay at your earliest convenience.

Sincerely,

How to Analyze Financial Statements

8C

Please follow the instruction below to correctly analyze financial Statement(s) when determining the financial capability of the Mortgagor, Sponsor, General Contractor, and or Manager.

A. Current Assets are cash and other assets convertible into cash during the normal operating cycle of business operations or 1 year, whichever is less.

1. When reviewing cash, take into consideration compensating balances, which would limit the amount of cash actually available.
2. Determine the current value of readily marketable stocks and bonds.
3. Evaluate the accounts receivable and classify the following as noncurrent.
   a. Amounts due from officers and employees.
   b. Amounts advanced to subsidiary, affiliated or associated companies.
   c. Disputed accounts receivable.
   d. Accounts receivable past due for more than 60 days. Funds from a local, State or Federal source past due beyond this period may be considered if evidence is provided that source is historically late and it can be expected that these funds will be received before initial closing.
4. Using a Schedule of Accounts Receivable by Age, determine if the amount allowed for doubtful accounts, if any, is adequate.
5. Recognize only syndication proceeds from other projects and notes receivable to be collected during the normal operating cycle or 1 year, whichever is less.
6. If the statement is audited, evaluate inventory and establish its liquidation value, relying on the accountant's review. Do not consider inventory, if statement is unaudited.
7. Recognize only prepaid expenses for the project.
8. Do not include:
   a. Equity in the proposed site, since consideration is given on Form HUD-92264-A, Part A.
   b. Cash equity in land and/or properties unless they are readily marketable and intended for the sale market.
   c. Anticipated profits from business ventures.
   d. Equities in real estate encumbered by high ratios of loan to value mortgages, unlisted stocks, goodwill, and other intangible assets.

B. Current liabilities are payables due during the normal operating period or 1 year, whichever is less.

1. Include as current liabilities, regardless of term, those relating to marketable land and completed properties that were treated as current assets.

   NOTE: If the balance sheet does not reflect the amounts required to complete construction in progress, the sponsor/general contractor must submit a supplementary statement of such

amounts, which contains the truth and accuracy certification referred to in Section 8.4 B 1 b.

2. Consider amounts due to officers, employees, affiliates or stockholders as current liabilities unless the obligations have a definite long-term maturity.
3. Consider amounts needed to satisfy broker's margin account (brokerage account allowing customers to buy securities with money borrowed from the broker).
4. Consider current portion of long-term liabilities.
5. Current year income tax payable. Normally, deferred income taxes are not considered current as long on the economic outlook of company does not appear to be in an adverse trend.
6. Do not include the amount outstanding on the project land, since this obligation is considered on Form HUD-92264-A, Part A.

C. Working Capital is the excess of current assets over current liabilities. If current liabilities exceed current assets, precede the difference with a minus sign to show a deficit.

D. Adjust the net working capital to consider:

1. Effects of contingent liabilities.
2. Financial needs of other projects in the planning stage or under construction.

E. Contingent Liability Related to Agreement for Payment of Real Property Taxes by Sponsor, Form FHA-1708. This agreement requires the sponsor to make a lump sum payment to cut the mortgage to an amount which could be carried by the mortgagor on a tax-paying basis if a project does not obtain or loses its abatement or exemption from real estate taxes in the future.

1. The execution of this Form is not required if tax exemption is granted based upon State legislation granting tax exemption to particular types of housing, e.g., housing located in urban renewal areas or housing for low and moderate income groups or for other social needs.
2. The execution of this Form is required for all insured projects if tax exemption is granted based upon general charitable statutes.
3. Treat this as a contingent liability when analyzing the Sponsor's financial statements.
4. If the Sponsor does not evidence the capacity to meet the financial requirements for closing plus this contingent liability, process on a tax-paying basis.
5. This requirement is not applicable to Section 202 or 811 projects in which the Field Counsel has concurred in the validity of the exemption based upon special legislation or general charitable statutes.

F. When a sponsor's financial interests are represented by a number of corporations:

1. Require a certification from the Board of Directors, which evidences their willingness to make the required funds available.

2. Establish the availability of funds from such corporations.
3. Consider whether:
   a. Individual corporations have any operating capital to spare.
   b. Laws under which they are incorporated and/or their banks permit:
      (1) Withdrawals, loans or advances to owners or sponsors.
      (2) Stock investment in affiliated corporations.
      (3) Guarantee of debts of associated corporations.
   c. In analyzing financial statement:
      (1) Do not consider interlocking debts, receivables and investments between all affiliated corporations.
      (2) Consider only those assets readily available for investment by the mortgagor.
      (3) Do not consider the operating capital and/or net worth of rental project holding corporations as assets available for closing.

G. <u>If funds are being provided by a parent company or affiliate of the sponsor:</u>

1. Require a certification from the Board of Directors or authorized agent which specifies the funds the parent company/affiliate is willing to commit.
2. Establish the availability of funds from parent company/affiliate.
3. Require the parent company/affiliate to submit a certification indicating that the lending institution will not make any claim against the mortgaged property, mortgage proceeds, any reserve or deposit required by HUD, or against the rents or other income from the mortgaged property for payment of the loan. This certification must contain the criminal warning reflected in Section 8.4 B b(3).

Appendix 11

HUD Initial Endorsement Diligence Review
Table of Contents

[redacted]

Appendix	Title
11A	Initial Endorsement Document Review – Architectural and Cost
11B	Initial Endorsement Document Review – Valuation
11C	Initial Endorsement Document Review – Mortgage Credit
11D	Initial Endorsement Document Review – Housing Program Representative
11D	Washington Docket

Initial Endorsement Document Review – Architectural and Cost

11A

PROJECT NAME: _____

PROJECT NUMBER: _____

Answer each question. Check "N/A" only where the document/question is not applicable to the project.

PART I. ARCHITECTURAL ANALYST REVIEW

	Yes	No	N/A
1. Request for Permission to commence Construction Prior to Initial Endorsement for Mortgage Insurance, Form FHA-2415, was executed.	__	__	__
If, yes			
a. Construction started and has been continuous.	__	__	__
If yes, construction started _____			
If no, comment: _____			
b. Additive or deductive change orders are in process or known to be proposed.	__	__	__
If yes, comment: _____			
c. No known problems, e.g.: nonpayment for work or material; liens; latent conditions; errors in the survey, drawings or specifications; wet site, strike, materials shortage, or other conditions delaying continued work; municipal stop order, other sanctions or requirements for additional work; contractor or subcontractor disputes, etc.	__	__	__
If yes, comment: _____			
d. Comments:_____			
2. Building Permits are for the proposed improvements, acceptable, unconditional, and current.	__	__	__

If no, comment: _____

_____

	Yes	No	N/A
3. Jurisdictional authority has given its stamp or permit, where applicable, for: storm water disposal, private water supply and sewage treatment/disposal facilities.	__	__	__

If no, comment: _____

_____

4. Assurance of Utilities

a. Water service letter is unconditional and reasonable in its currency.	__	__	__

If no, comment: _____

_____

b. Sanitary sewer service letter is unconditional and is reasonable in its currency.	__	__	__

If no, comment: _____

_____

c. Electric service letter is unconditional and is reasonable in its currency.	__	__	__

If no, comment: _____

_____

d. Gas service letter is unconditional and is reasonable in its currency.	__	__	__

If no, comment: _____

_____

e. District heat letter is unconditional and is reasonable in its currency.	__	__	__

If no, comment: _____

_____

f. Telephone service letter is unconditional and is reasonable in its currency.	__	__	__

If no, comment: _____

_____

	Yes	No	N/A
g. Cable TV letter is unconditional and is reasonable in its currency.	__	__	__

If no, comment: _____

_____

5. Survey, Surveyor's Certificate and Title Policy.

a. The title policy/endorsement matches the legal description on the survey.	__	__	__

If no, comment: _____

_____

b. Easements, encroachments and other title policy/endorsement Schedule B identified exceptions are consistent with and between the plat for recordation/survey, surveyor's certificate, site plan and other drawings.	__	__	__

If no, comment: _____

_____

c. Easements across other sites for project driveways, drainage outfalls, etc., are acceptably reflected in plats for recordation, and covered by maintenance agreements where used jointly with others.	__	__	__

If yes, identify: _____

_____

If no, comment: _____

_____

d. The Surveyor's Certificate is dated and is acceptable.	__	__	__

If no, comment: _____

_____

e. The last Survey revision date is _____ and the survey is acceptable.	__	__	__

If no, comment: _____

_____

	Yes	No	N/A
f. Air rights map applies.	__	__	__
If yes:			
1) It provides vertical ways to grade for vertical transportation, emergency exits, utilities, trash chutes, etc.			
If no, comment _____			
2) It provides necessary easements for exterior and interior ingress and egress, emergency exit discharge, services, maintenance, etc.	__	__	__
If no, comment: _____			
3) Maintenance agreements cover all facilities jointly used with others.	__	__	__
If yes, identify: _____			
If no, comment: _____			

6. Construction Documents.

a. The drawings and specifications, including drawing dates and revision dates, conform to those accepted for firm commitment.	__	__	__
If no:			
1) Revisions are minor, dictated by issues arising after firm, and don't affect construction costs or project value.	__	__	__
If no, comment: _____			
2) Revised sheets and pages have been inserted in the drawings and specifications and are acceptable.	__	__	__

If no, comment: _____

_____

	Yes	No	N/A
3) Addenda and attachments required for changes from the firm commitment drawings and specifications are included in the project manual.	__	__	__

If yes, they are numbered _____

and dated _____

If no, comment: _____

_____

	Yes	No	N/A
4) Reprocessing is required, due to changes from the drawings and specifications upon which the commitment was issued.	__	__	__

If yes, comment: _____

_____

5)Comments:_____

_____

_____

_____

_____

	Yes	No	N/A
b. The Master Set and Sets 2 and 3 are signed and initialed as per Section 5.7.C.	__	__	__

If no, comment: _____

_____

	Yes	No	N/A
c. The correct wage decision is incorporated in the project manual.	__	__	__

If no, the following are required:_____

_____

	Yes	No	N/A
d. The wage rate is a special determination.	__	__	__

If yes, expiration date is: _____

7. Construction Contract

	Yes	No	N/A
a. Drawing sheets, specification pages, and if applicable, addenda numbers and pages, are properly identified.	__	__	__

If no, the corrected list/index is attached.

b. The design architect(s) and supervisory architect are correctly listed.	__	__	__

If no, comment: _____

_____

c. The amendment to the construction contract for Identities of Interest Between the Contractor, Owner and Architect is attached.	__	__	__

If no, comment: _____

_____

d. The amendment to the construction contract for Payment for Components Stored Offsite, if applicable, is attached.	__	__	__

If no, comment: _____

_____

8. Offsite work is involved.	__	__	__

If yes:

a. The municipal jurisdiction's installation assurance letter is unconditional and reasonable in its currency.	__	__	__

If no, comment: _____

_____

If N/A, completion assurance is required for the following:

_____

_____

b. Construction contract(s) is/are acceptable.	__	__	__

If yes, identify the contract(s) and work: _____

_____

If no, comment: _____

_____

c. Drawings and specifications are:

1) Included in the construction documents for on-site work and are acceptably segregated by contract limit lines and divisions of the specifications. __ Yes __ No __ N/A

If no, comment:_____

_____

2) Included in separate drawings and specifications from on-site work. __ __ __

If yes, identify:_____

_____

_____

3) Comment: _____

_____

_____

9. Owner/Architect Agreement(s)

a. The prime architect(s) is/are:

b. There is an agreement, B108, for each prime architect. __ __ __

If no, comment: _____

_____

c. The HUD amendment to the B108 is referenced in Article 12 of, and attached to each Owner/Architect Agreement. __ __ __

If no, comment: _____

_____

d. Each B108 identifies the specific services to be performed by the applicable prime architect. __ __ __

If no, comment: _____

_____

e. Article 11 is acceptable for each B108, and all referenced appendices, addenda, etc., are attached. __ __ __

If no, comment: _____

_____

f. Addendum to Owner-Arch Agreement and/or Construction Contract show(s) an identity of interest for Supervisory Arch. __ __ __

If yes, comment: _____

_____

	Yes	No	N/A
g. Comment:_____			

10. Special Conditions of the Commitment, numbered _____, are considered in this review. Required documents have been submitted and found acceptable for them all. __ __ __

a. Special Conditions numbered _____ have not been satisfied.

Comment: _____

_____

b. The following documents must be submitted:

_____

_____

11. The list(s) of major movable equipment is/are acceptable, which applicable to Sect 221d SRO, 2311 232, and 242 projects.

If no, comment: _____

_____

12. Comment:

_____

_____

_____

PART II. COST ANALYST REVIEW

13. Two copies of the property insurance requirements are attached and acceptable.	__	__	__

If no, comment: _____

_____

14. Agreement and Certification.

a. The amounts shown on the Agreement and Certification are correct.	__	__	__

If no, the following are the correct amounts:

_____

_____

	Yes	No	N/A
b. The contract, including dollar amounts for general overhead and profit has been approved for each identity of interest subcontractor listed in the Certification and Agreement and the Amendment to the Construction Contract.	__	__	__

If no, comment: _____

_____

15. Construction Contract.

a. A signed approved cost breakdown, Form HUD-2328, is attached as Exhibit A to the Construction Contract.	__	__	__

If no, comment: _____

_____

b. The Inventory and Cost Breakdown for Stored Components, if applicable, is acceptable and attached to Form HUD-2328, Exhibit A to the Construction Contract.	__	__	__

If no, comment: _ _____

_____

	Yes	No	N/A
c. The construction contract price is correct.	__	__	__
If no, the correct amount is _____			
d. The contract completion date is correct, and if an early start, reflects Form FHA-2415 modification requirements.	__	__	__
If no, the completion date should be _____			
e. The contract addendum lists identities of interest indicating the need for pre-approval of subcontractor contracts for general overhead and profit.	__	__	__
If yes, comment: _____ _____			
16. Progress Schedule agrees with the Contract time and is acceptable.	__	__	__
If no, comment: _____ _____			
17. Assurance of completion for offsite work not done by municipality is required.	__	__	__

	Yes	No	N/A
If yes, for the following contracts and costs.			
_____ $_____			
_____ $_____			
_____ $_____			
18. The Mortgagor's and Architect's Certificate(s) is/are consistent with the B108(s) for prime architects, and Other A&E Fees are reasonable.	__	__	__
If no, comment: _____ _____			

19. Special Conditions of the Commitment numbered_____, are considered in this review. Required documents have been submitted and found acceptable for them all. __ __ __

If no:

a. Special Conditions numbered _____have not been satisfied.
Comment: _____

_____

b. The following documents must be submitted;

_____

_____

b. Listed chattel and values are acceptable for the Financial Statement and Security Agreement (UCC) __ __ __

If no, comment: _____

_____

c. Listed chattel and values are acceptable for the Chattel Mortgage. __ __ __

If no, comment _____

_____

20. Comments:

_____

_____

_____

_____

_____

_____

_____

_____ _____

ARCHITECTURAL ANALYST DATE

_____ _____

COST ANALYST DATE

_____ _____

CHIEF ARCHITECTURE AND COST DATE

Initial Endorsement Document Review – Valuation

11B

PROJECT NAME: _____

PROJECT NUMBER: _____

Answer each question. Check "N/A" only where the document/question is not applicable to the project.

	Yes	No	N/A
1. Environmental assessment has been approved, copy attached, and all exceptions cleared.	__	__	__
If no, comment: _____			
2. Survey and Surveyor's Certificate.	__	__	__
a. The property surveyed is the same as that which was appraised.			
If no, comment: _____			
b. A difference in site area affects net value.	__	__	__
If yes, comment: _____			
c. Review of the Survey and Surveyor's Certificate reveals encroachments not previously considered	__	__	__
If yes, comment: _____			
d. Encroachments are acceptable and do not affect value and marketability.	__	__	__
If no, comment: _____			
The following encroachments must be removed prior to closing: _____			
f. Flood hazard elevations shown on the survey are consistent with environmental assessment clearance assumptions.	__	__	__
	Yes	No	N/A

If no, comment: _____

_____

g. Reprocessing is required because of Survey or Surveyor's Certificate identified issues. __ __ __

If yes, comment: _____

_____

3. Maintenance agreements have been considered in project operating expense. __ __ __

a. If no, processing is required.

b. Comment:

_____

_____

4. Zoning Compliance is unconditional and is reasonable in its currency. __ __ __

If no, comment: _____

_____

5. The lease and is acceptable (leasehold projects only). __ __ __

If no, the following changes must be made:

_____

_____

6. Special Conditions of the Commitment, numbered _____, are considered in this review. Required documents have been submitted and found Acceptable for them all. __ __ __

If no:

a. Special Conditions numbered _____have not been satisfied.

Comment: _____

_____

Yes No N/A

b. The following documents must be submitted:

_____

_____

7. Owner's certification listing all federal/state/local government insurance, loan, grant, tax credit, or subsidy programs in which the project/owner will participate and any grants or below-market loans to be received from non-governmental sources is on file (required for all projects). __ __ __

a. If no, comment:

_____

_____

b. If yes, certification is consistent with valuation processing and deed covenant restrictions. __ __ __

If no, comment: _____

_____

8. Owner's Sources and Uses of Funds Statement is on file listing: all funds available; all purposes for which funds will be disbursed; and dates any investor contributions are due. __ __ __

If no, comment: _____

_____

9. Deed covenants or other closing documents include low-income occupancy and/or rent restrictions. __ __ __

a. If yes:

The basis is: tax credits or tax-exempt bonds (Section 142 d) or tax-exempt bonds (State or local) or local rent restrictions (identify which).

Comment: _____

_____

The deed covenant, and/or other closing document, low-income occupancy and/or rent restrictions are consistent with the IRS tax credit allocation certification, IRS tax-exempt ruling, etc., as applicable, and the assumptions used in valuation processing.

b. If local rent restrictions, then project assistance is provided in the form of: tax exempt bands or CDGB or land write down. __ __ __

Yes No N/A

If yes, identify which:

_____

_____

If no, comment: _____

_____

Certification for providing the assistance is included and consistent with the restrictions. __ __ __

If yes, identify form of assistance certification:

_____

_____

If no, comment: _____

_____

c. More than 40 percent of units are subject to low- income occupancy and/or rent restrictions under tax exempt bond or tax credit financing provisions. __ __ __

If yes, project is assisted by project based Section 8 subsidy or comparable long-term state/local subsidy.

The basis is: tax credits or tax-exempt bonds (Section 142 d) or tax-exempt bonds (State or local) or local rent restrictions (identify which).

Comment: _____

_____

The deed covenant, and/or other closing document, low-income occupancy and/or rent restrictions are consistent with the IRS tax credit allocation certification, IRS tax-exempt ruling, etc., as applicable, and the assumptions used in valuation processing. __ __ __

If no, comment: _____

_____

d. If local rent restrictions, then project assistance is provided in the form of: tax exempt bands or CDGB or land write down. __ __ __

If yes, identify which:

_____

_____

Yes No N/A

If no, comment: _____

_____

Certification for providing the assistance is included and consistent with the restrictions. __ __ __

If yes, identify form of assistance certification:

_____

_____

If no, comment: _____

_____

e. More than 40 percent of units are subject to low- income occupancy and/or rent restrictions under tax-exempt bond or tax credit financing provisions. __ __ __

If yes, project is assisted by project based Section 8 subsidy or comparable long-term state/local subsidy, or Headquarters approval letter is on file. __ __ __

If yes, identify which:

_____

_____

If no, comment: _____

_____

10. Title Policy/Endorsement Schedule B Items and/or other identified title exceptions have been considered in project value and marketability or have no effect on them. __ __ __

If no:

a. Reprocessing is required, if the following items/exceptions are not removed:

_____

Comment: _____

_____

b. The following items/exceptions must be removed under any circumstances:

_____

_____

Comment:_____

11. Comments:

_____

_____

_____

_____	_____
APPRAISER	CHIEF APPRAISER
_____	_____
Date	Date

Initial Endorsement Document Review – Mortgage Credit

11C

PROJECT NAME: _____

PROJECT NUMBER:_____

Answer each question. Check "N/A" only where the document/question is not applicable to the project.

	Yes	No	N/A
1. Request for Permission to Commence construction prior to Initial Endorsement for Mortgage Insurance, Form FHA-2415, was executed.	__	__	__
If yes:			
a. Release of liens by the contractor and subcontractors are acceptable.	__	__	__
If no, comment: _____ _____			
b. The commitment date for the start of principal payment has been modified to reflect the early start of construction.	__	__	__
If no, comment: _____ _____			
c. Provisions have been made to escrow funds for additive change orders approved during the early start of construction but not yet completed and/or paid.	__	__	__
If no, comment: _____ _____			
d. Mortgagor/Contractor Agreement to recognize interest costs relating to early start submitted.	__	__	__
If no, comment: _____ _____			
2. The request for an initial advance is acceptable and funds requested under the construction contract, including any for work under an early start, are supported by a Contractor's Requisition, Form HUD-92448.	__	__	__

If no, comment: _____

_____

	Yes	No	N/A
3. 2530 Clearances.			
a. The mortgagor entity has been cleared pursuant to Form HUD-2530 procedures.	__	__	__
If no, comment and steps taken: _____ _____			
b. Individuals or entities shown in the corporate charter, partnership agreement or incumbency certificate have been cleared pursuant to Form HUD-2530 procedures.	__	__	__
If no: The following need clearance: _____ _____			
Actions taken: _____ _____			
c. Individuals or entities shown on the contractor's certification have been approved pursuant to Form HUD-2530 procedures.	__	__	__
If no: The following need clearance: _____ _____			
d. All architects and attorneys who have an identity of interest have been cleared pursuant to Form HUD 2530 procedures.	__	__	__

	Yes	No	N/A
If no: The following need clearance: _____ _____			
e. All identified packagers, consultants, project managers and management agents have been cleared pursuant to 2530 procedures.	__	__	__
If no: The following need clearance: _____ _____			

4.Partnership Agreement:

a. Credit check, financial review and 2530 clearance are acceptable for each principal partner.	__	__	__
If no, comment: _____ _____			
b. Rights and duties of each partner are acceptable.	__	__	__
If no, comment: _____ _____			
c. Capital investment made/maintained for each partner is acceptable.	__	__	__
If no, comment: _____ _____			
d. Partnership term equals or exceeds mortgage term.	__	__	__
If no, partnership term must be: _____			
e. Mortgagor is a single asset mortgagor.	__	__	__
If no, comment: _____ _____			

	Yes	No	N/A
f. Partnership Agreement is consistent with the Regulatory Agreement.	__	__	__
If no, comment: _____			
g. The partnership agreement improperly provides for the mortgagor to indemnify partners and officers against lawsuits.	__	__	__
If yes, comment: _____			
h. Comments:			

5. Corporate Mortgagor.

a. Credit check, financial review and 2530 clearance are acceptable for each principal investor.	__	__	__
If no, comment: _____			
b. Mortgagor is a single asset mortgagor.	__	__	__
If no, comment: _____			
c. The articles of incorporation and bylaws are consistent with the Regulatory Agreement and other documents.	__	__	__
If no, comment: _____			
d. The articles of incorporation and/or by-laws improperly provide for the mortgagor to indemnify board members against suits.	__	__	__
If yes, comment: _____			

6. The Agreement and certification is acceptable.	__	__	__
	Yes	No	N/A

If no, comment: _____

_____

7. The amount shown in the Regulatory Agreement for the Reserve Fund for Replacements is correct. __ __ __

If no, the correct amount is _____

8. Construction Contract.

a. The time for construction is correct. __ __ __

If no, comment: _____

_____

b. The amount shown for liquidated damages is correct. __ __ __

If no, the correct amount is _____

c. The contract price agrees with the 2328. __ __ __

If no, the correct amount is _____

d. The cash upset amount is correct. __ __ __

If no, the correct amount is _____

e. The Construction Contract Incentive Payment in Article 3 is acceptable in language, amount and computation. __ __ __

If no, comment: _____

_____

f. The Note amount is approved, if payment is by other than cash. __ __ __

If no, the correct amount is _____

g. Assurance of completion amount shown in Article 6 is correct. __ __ __

If no, the correct amount is _____

h. The Cost Breakdown (Form HUD-2328) has been confirmed correct by Arch/Cost. __ __ __

If no, comment: _____

_____

i. The filing period for monthly advances is acceptable. __ __ __

	Yes	No	N/A
If no, comment: _____			
j. The Amendment to the construction contract for identities of interest is attached and acceptable.	__	__	__
If no, comment: _____			
9. Advances for Components Stored Offsite are involved.	__	__	__
If yes:			
a. Corporate surety bonds are 100 percent each for performance and payment and are acceptable.	__	__	__
If no, comment: _____			
b. The Inventory and Cost Breakdown for Stored Components is attached to Form HUD-2328, Exhibit A to the Construction contract.	__	__	__
If no, comment: _____			
c. The construction contract includes the addendum for offsite storage.	__	__	__
If no, comment: _____			
10. Assurance of Completion for on-site work.			
a. The performance and payment bond(s) are for100 percent each.	__	__	__
If no, comment: _____			
b. The bonding company, _____ _____, is acceptable to write a policy in the stated amount.			

If no, maximum policy amount is _____

	Yes	No	N/A
c. Completion Assurance Agreement is correct.	__	__	__
If no, the correct amount is _____			
d. Personal Undertaking, Form FHA-2459, is acceptable and in the correct amount.	__	__	__
If no, comment: _____			
e. Comment: _____			
11. The Assurance of Completion for offsite work is acceptable.	__	__	__
If no, comment: _____			
12. Owner-Architect Agreement fees and FormHUD-92403-1 agree for each design architect.	__	__	__
If no, comment: _____			
13. The Certificate of Architectural/Engineering Fees agrees with prime architect contract fees and other A&E fee claims.	__	__	__
If no, comment: _____			
14. Mortgage Note or Rider.			
a. The interest rate is the same as shown on the commitment.	__	__	__
If no, the correct rate is _____			
b. The Mortgage amount is correct.	__	__	__
If no, the correct amount is _____			
c. The P&I is correct.	__	__	__
If no, the correct amount is _____			

d. The Commencement of Amortization date is correct. __ __ __

	Yes	No	N/A
If no, the correct date is _____			
e. The ending date for amortization is correct.	__	__	__
If no, the correct date is _____			
f. The Special Provisions are consistent with other reviewed documents and financing criteria.	__	__	__

If no, comment: _____

_____

g. Comments:

_____

_____

15. Mortgage or Mortgage Modification Agreement.

a. The interest rate is the same as shown on the commitment.	__	__	__
If no, the correct rate is _____			
b. The Mortgage amount is correct.	__	__	__
If no, the correct amount is _____			
c. The P&I is correct.	__	__	__
If no, the correct amount is _____			
d. The Commencement of Amortization date is correct.	__	__	__
If no, the correct date is _____			
e. The ending date for amortization is correct.	__	__	__
If no, the correct date is _____			
f. The Special Provisions are consistent with other reviewed documents and program financing criteria.	__	__	__

If no, comment:

g. Comments:

_____

_____

_____

	Yes	No	N/A
16. Title Policy or Endorsement.			
a. Policy amount is _____ which equals or exceeds the mortgage.	__	__	__
If no, comment: _____ _____			
b. The title company, _____ is acceptable for a policy in that amount.	__	__	__
If no, comment: _____ _____			
17. The Building Loan Agreement is acceptable.	__	__	__
If no, the following changes are required: _____ _____			
18. The Mortgagee's Certificate is acceptable as to fees, discounts, notes, and other terms, and agrees with firm commitment processing.	__	__	__
If no, the following changes are required: _____ _____			
19. The Sponsor's Certification, Form FHA-3437, for 231 NP proposals is acceptable	__	__	__
If no, comment: _____ _____			
20. The Guaranty Agreement, for 12-Month Debt Service Escrow for B&C Independent Living Units is acceptable.	__	__	__
If no, comment: _____ _____			

	Yes	No	N/A
21. The Financial Requirements For Closing, Form FHA 2283, is attached.	__	__	__
If no, comment: _____ _____			
22. Special Conditions of the Commitment numbered_____ are considered in this review. Required documents have been submitted and found acceptable for them all.	__	__	__
If no:			
a. Special Conditions numbered _____have not been satisfied.			
b. The following documents must be submitted: _____ _____			
c. The following actions have been taken: _____ _____			
23. Evidence that the mortgagor is able to finance its required minimum financial investment is acceptable.	__	__	__
If no, comment: _____ _____			

_____

Mortgage Credit Examiner

_____

Date

Note: The Hub Director is responsible for securing corrected initial draw documents directly from the mortgagee.

Initial Endorsement Document Review – Housing Program Representative

11D

PROJECT NAME: _____

PROJECTNUMBER: _____

Answer each question. Check N/A only where the document/question is not applicable to the project.

	Yes	No	N/A
1. The commitment issuance and expiration dates are_____ and _____ respectively.			
a. The commitment has been extended	__	__	__
If yes, the new expiration date is: _____			
b. The commitment has been reopened	__	__	__
If yes, the new expiration date is: _____			
c. The commitment has been amended.	__	__	__
If yes, the amendment dates are: _____			
2. The Commitment has been assigned.	__	__	__
If yes:			
a. The new mortgagee is an approved mortgagee and the assignment is acceptable.	__	__	__
If no, comment: _____ _____			
b. Current mortgagee:_____ Mortgagee number: _____			
c. Previous mortgagee: _____ Mortgagee number: _____			
3. Special conditions of the Firm Commitment are No. _____ thru _____ inclusively.			

	Yes	No	N/A

a. Architectural, Cost, Valuation, and Mortgage Credit reviews address Nos. _____, _____, _____ and _____ respectively.

b. This review considers special conditions Nos. _____. Documents have been submitted and found acceptable for them all. __ __ __

If no, comment:_____

c. Special conditions numbered _____have not been satisfied.

Comment: _____

_____

d. The following documents must be submitted:

_____

_____

e. The following actions have been taken:

_____

_____

4. Request For Permission to Commence Construction Prior to Initial Endorsement for Mortgage Insurance, Form FHA 2415, was executed.

If yes: __ __ __

a. Copies were furnished to Arch and MC, and construction started.

If no, comment:

_____

_____

b. All known issues arising from the early start have been reconciled. __ __ __

Yes No N/A

If no, comment: _____

_____

5. EO 12372 Clearance, if applicable, has been received.

6. Chronology of Mortgage Transactions, Form FHA 260, is attached. __ __ __

If no, comment: _____

_____

7. Checks in the amount of $ _____ for_____, and $ _____ for _____ _____ must be collected at closing.

8. Owner's certification listing all Federal/State/local government insurance, loan, grant or subsidy programs in which the project/owner will participate and any grants or below market loans to be received from non-government sources is signed and on file (required for all projects). __ __ __

If no, comment: _____

_____

9. The following documents, if applicable, have been signed and returned by the PHA/Owner:

a. Annual Contributions Contract (ACC). __ __ __

If no, comment: _____

_____

b. Agreement to Enter into a Housing Assistance Payment Contract (AHAP). __ __ __

If no, comment: _____

_____

c. Housing Assistance Payment Contract (HAP). __ __ __

If no, comment: _____

_____

d. Low-Income Housing Tax Credit or Historic Tax Credit Allocation

Yes No N/A

Certification, IRS Form 8609 or IRS Form 3468, HQ review, Exhibits 1-7, and owner's statement agreeing to notify HUD of any changes. __ __ __

If no, comment: _____

_____

e. Owner's Certification That Project Will Not Participate in the Low Income Housing Tax Credit (LIHTC) Program. __ __ __

If no, comment: _____

_____

f. IRS tax exemption ruling. __ __ __

If no, comment: _____

_____

g. Other.

_____

_____

_____

10. COMMENTS:

_____

_____

_____

PROGRAM REVIEWER _____

SUPERVISOR _____

DATE _____

HUD Washington Docket 11E

I. Initial Preparation of the Washington and Field Office Dockets is the responsibility of the Director of Housing Development.

A. Assign appropriate staff in time to complete initial preparation of the Washington Docket and Field Office Docket. Include and arrange the documents, except for those used at final endorsement/endorsement, according to paragraphs II.B.1 and III.A.

B. Certify as Complete and Deliver the arranged documents for both the Washington Docket and Field Office Docket to the Hub/Program Center Director designee for Docket completion and distribution.

II. Washington Docket.

A. Hub/Program Center Director is responsible for:

1. Designating a person to complete the Washington Docket, i.e., combining the documents provided by the Director, Housing Development and the final closing/closing documents furnished by the closing attorney.

2. Assuring that the Washington Docket is reviewed by the closing attorney and that the closing attorney includes the certificate attesting to the completeness and accuracy of the closing documents incorporated into the Docket.

3. Its transmittal to Headquarters' Chief, Records Management, HRDC, Department of Housing and Urban Development, Room B264, 451 Seventh Street, SW, Washington, DC 20410, within 30 working days of the closing.

    a. Waiver requests for delayed shipping must be supported and secured from the Director, Office of Multifamily Housing Development, HTD.

    b. The existence of outstanding escrows is not a basis for delaying submission of the docket.

B. Hub/ Program Center Director's Designee is responsible for:

1. Verifying that all applicable project documents are filed in the Washington Docket by the categories and sequence listed in the *Schedule of Washington Docket Contents* below.

2. Delivering the Washington Docket to the closing attorney for certification, and after certification transmitting the Docket under the Director's memorandum to the Chief, Records Management, HRDC.

3. Sending a copy of the transmittal memorandum to each of the following:

    a. Director, Housing Development Division and Director, Housing Asset Management Division; and

b. Headquarters Director, Management Services Division, HFMP, Room 9118, and Director, Multifamily Accounting & Servicing Division, HOAM, Room 6258.

C. HUD Closing Attorney is responsible for reviewing the assembled Washington Docket and:

1. Certifying to any form revisions as provided for in Handbook 4430.1 REV-1, paragraph 1-7 and MAP Guide Chapter 4 Section 4.1.E, (see the *Schedule of Washington Docket Contents* for certification),

2. Certifying that all closing documents are included in the Washington Docket, including the initial closing documents where applicable, and explaining any deviations,

3. Including the certification in the Washington Docket, below, and

4. Returning the Washington Docket to the Hub/Program Center Director's designee for distribution according to paragraph B. above.

D. Recordation and Safekeeping. The Chief, Records Management, OAMS, is responsible for:

1. Maintaining the Washington Docket for the mortgage term plus 6 years as provided in Handbook 2225.6 REV-1, HUD Records Disposition Schedules; and

2. Notifying the Hub/Program Center Director of Docket receipt.

E. Washington Docket Addenda. Where outstanding escrows exist when the Washington Docket is shipped, or there are modifications/ allonges, the Hub/Program Center is responsible for the subsequent shipment of germane documents to the Chief, Records Management, HRDC.

1. Prepare, certify and ship any addenda in the same manner as prescribed for the Docket, except identify on the transmittal memorandum and *Schedule of Washington Docket Contents* that the documents are an addendum to the Washington Docket.

2. Transmit addenda within 30 days after all escrows are closed, or modifications/ allonges completed.

F. Construction Documents are a supplement to the Washington Docket and consist of the:

1. Master Set of Drawings and Specifications; and

2. Original copy of all approved Construction Changes, For HUD–92437, Architects Supplement Instructions, AIA Document G710, and supporting exhibits.

G. Preparation for/and Shipment of Construction Documents. The Chief of Architecture/

Engineering & Cost is responsible for assembling and preparing the documents for shipment to the Regional Records Center, and certifying to document completeness on in the transmittal memorandum, B. 3., above.

1. Retain the Construction Documents in the Hub/Program Center for one (1) year after final endorsement and at the Records Center as provided in Handbook 2225.6 REV-1, Schedule 1. Document shipment may be deferred up to one (1) additional year after final endorsement to allow concurrent shipment of documents for several projects.

2. Secure the Change Orders, Architect's Supplemental Instructions, and supporting documents with rubber bands or twine and roll all documents into the drawings. Secure the roll with twine and affix a copy of transmittal memorandum B.3., above.

3. Label/code the documents and/or packing cartons in accordance with Handbook 2228.1 REV-3, Records Disposition Management.

H. Washington Docket Integration.

1. The Hub/Program Center Director's designee is responsible for forwarding the following construction document information to the Chief, Records Management, HRDC, Room B264:

a. Copy of transmittal memorandum that states the Chief, Architecture/ Engineering & Cost certify to document completeness.

b. Regional Records Center address, and packing box and/or document retrieval identification number or code.

2. The Chief, Records Management is responsible for:

a. Acknowledging receipt of documents to the Hub/Program Center Director.

b. Incorporating the Chief, Architecture/ Engineering & Cost document completeness certification (transmittal memorandum copy), and the construction document storage retrieval address and identification code into the Washington Docket.

III. Field Office Docket is a duplicate of the Washington Docket plus any additional correspondence and documents remaining after making up the Washington Docket.

A. File Preparation.

1. Number the Field Office Docket Binders, 1 of N, 2 of N, etc., where "N" equals the `total number of binders where project document bulk requires multiple binders.

2. Arrange the documents in closing checklist order on the right side of the binders. Related correspondence and supporting reports, exhibits, etc., may be filed chronologically with the documents or on the left side of the binders.

3. Forward the file to the Hub/Program Center Director's designee in accordance with

paragraph I above for the addition of the final endorsement/ endorsement documents, and transmittal to the Director, Housing Asset Management.

B. File Maintenance/Disposition. The Director of Housing Asset Management is responsible for:

1. Maintaining the Field Office Docket for Housing Asset Management and any Housing Development staff use after final endorsement/endorsement.

2. Disposition of the Field Office Docket in accordance with Handbook 2225.6, HUD Records Disposition Schedule.

IV. Amortization Schedule (Multifamily Mortgage). Submit the following documents within five (5) working days of closing to the Multifamily Insurance Operations Branch, MFIOB, Department of Housing and Urban Development, P.O. Box 44124,Washington, DC 20026-4124.

A. Insured Advances Projects. Form HUD-290, Closing Memorandum; Form HUD-92023, Request for Final Endorsement of Credit Instrument; Form HUD-2580, Maximum Insurable Mortgage; Deed of Trust Note; and any modifications, riders or allonges.

B. Insurance Upon Completion Projects. Form HUD-290, Closing Memorandum; and Form HUD-27038, Official Receipt of Federal Housing Administration (of the initial premium).

C. Projects Pursuant to Section 223(f). Form HUD-290, Closing Memorandum; and Form HUD-27038, Official Receipt of Federal Housing Administration (of the initial premium).

D. Distribution. The Multifamily Insurance Operations Branch, MFIOB, will audit the case, prepare the amortization schedule, and transmit copies as follows:

1. Requisitioning Field Office, for inclusion in the Washington Docket and Field Office Docket,

2. Current lending servicer,

3. Multifamily Insurance Operation Branch's active project file.

SCHEDULE OF WASHINGTON DOCKET CONTENTS

HUD Office: _____ Mortgagor: _____

Project Name: _____

_____

Project No: _____

Proposed: _____ Sub Rehab: _____ (Existing) Refinance: _____ Purchase: _____

Section of Act: _____ Compiled By: _____

Endorsement Date: _____ Date Completed: _____

==========

The HUD Closing Attorney's Certification for the Washington Docket's completeness, Notes to the sections, the Washington Docket Completeness Instructions with the indicated document type (i.e. original (O), certified (C), extra copy (EC), etc.) are at the end of this schedule.

==========

The following eight (8) sections identify the forms and documents that create the docket content:

Application
Contract
Title
Mortgage
Corporate
Fiscal
Closing
Mortgage Credit Control Files for left side of docket

APPLICATION SECTION

Format	Seed Money Information	(C)
Format	Keys Amendment Section 1616(e) of the Social Security Act	(O)
HUD-2576HF	Certificate of Need. (242) (or alternate Market Study, if applicable)	(O)
HUD-92013	* Application for Mortgage Insurance (SAMA/Feasibility/Conditional/Firm) (See Note Section No.1)	(O)
HUD-92013-E	Supplemental Application and Processing Form, Housing for the Elderly	(C)
HUD-92013-SUPP	Application - Project Mortgage Insurance (Supplement to HUD-92013)	(O)
HUD-92264	* Project Analysis (for Firm Commitment, and Conditional Commitment and SAMA or Feasibility Letter, if applicable, including all revisions and amendments)	(C)
HUD-92264-A	Supplement to Project Income Analysis and Appraisal	(C)
Format	Compute Fees in a Purchase Transaction (223(f)	(O)
Format	Compute Fees in a Refinance Transaction (223(f))	(O)
Format	Compute Operating Deficit Escrow (223(f))	(O)
HUD-92438	Underwriting Summary Report	(O)
HUD-92432	Firm Commitment for Insurance of Advances; and Conditional Commitment and SAMA or Feasibility Letter, if applicable (See Note Section No. 2 below)	(C)
FHA-2453	* Firm Commitment to Insure Upon Completion; and Conditional Commitment and SAMA or Feasibility Letter, if applicable. (See Note Section No. 2 below)	(C)
Format	Firm Commitment Existing and Conditional if applicable (see Note Section No. 2 below)	(C)
Format	Certification re: Fulfillment of Special Conditions of Commitment (if any)	(O)
Format	Assignment of Commitment (if any)	(EC)
Format	FNMA/GNMA Commitment (if any)	(EC)
HUD-9447	Unit Vacancy and Resident Turnover Report	(O)

HUD-9449	Monthly Resident Roster/Accommodation Charge	(O)
HUD-9450	Computation of Term and Principal and Interest Payment for Section 223(f) Projects in Older, Declining Areas	(O)
HUD-2530	Previous Participation Certificate	(EC)
Form	Management Review Questionnaire	(O)
HUD-92415	Request for Permission to Commence Construction Prior to Initial Endorsement	(O)
HUD-92403-1	Mortgagor's and Architect's Certificate	(O)
HUD-92403	Application for Insurance of Advance of Mortgage Proceeds (See Note Section No. 3 below)	(EC)
HUD-92448	Contractor's Requisition Project Mortgages	(EC)
Format	HUD Representative's Memoranda accepting offsite and other escrowed work for release of escrowed funds	(O)
HUD-92023	Request for Final Endorsement of Credit Instrument (See Note Section No. 4 below)	(O)
HUD-92010	Equal Employment Opportunity Certificate	(O)
HUD-3305	Agreement and Certification (Insurance of Advances Projects with No Profit and Risk Allowance)	(O)
HUD-3306	Agreement and Certification (Insurance Upon Completion Projects)	(O)
HUD-3433	Request for Determination of Eligibility as Non-profit Sponsor and/or Mortgagor	(O)
HUD-3434	Certificate of Relationships and Nonprofit Motives (221(d)(3),231, and 236)	(O)
HUD-3435	Certification Regarding Contractual Relationships on Nonprofit Motives (221(d)(4) and 231)	(O)
FHA-3476	Certificate of Eligibility Under Section 221 (Persons displaced)	(O)
HUD-92451	Financial Record of Mortgage Loan Transaction	(O)
HUD-58047	Report of Default During Construction (Before Final Endorsement)	(O)
HUD-4128	Environmental Assessment for Subdivision and Multifamily Project (for new construction)	(O)
HUD-4128.1	Compliance a d LAC Conditions Record (for Substantial Rehabilitation or Existing Projects)	(O)

Format	Draft Environmental Impact Statement (if required)	(O)
Format	Final Environmental Impact Statement (if required)	(O)
SF-424	Application for Federal Assistance (Intergovernmental Review)	(C)
HUD-935.2A	Affirmative Fair Housing Marketing Plan (Multifamily)	(O)
HUD-5379	HUD Representatives Trip Report	(C)
HUD-92458	Rent Schedule Low Rent Housing	(C)

CONTRACT SECTION

HUD-92441	Building Loan Agreement	(EC)
FHA-2441-SUP	Addendum to Building Loan Agreement (HUD-92441)	(EC)
HUD-92442	Construction Contract – Lump Sum	(EC)
HUD-92442-A	Construction Contract – Cost Plus	(EC)
HUD-92443	Construction Contract Incentive Payment	(EC)
Format	Building Permits	(C)
HUD-92452	Performance Bond – Dual Obligee	(EC)
HUD-92452-A	Payment Bond – Dual Obligee	(EC)
HUD-92450	Completion Assurance Agreement	(EC)
FHA-2477	Bond Guaranteeing Sponsor's Performance	(EC)
FHA-2459	Personal Undertaking (Indemnity Agreement)	(EC)
Format	Assurance from Public Authorities or Public Utility Companies of Installation of Off-Site Facilities (if any), (or)	(EC)
FHA-2479	Off-Site Bond, (or)	(DO)
HUD-92464	Escrow Agreement for Off-Site Faculties	(EC)
HUD-3259	Surety Bond Against Defects Due to Defective Materials and/or Faulty Workmanship	(EC)
HUD-92464	Request for Approval of Advance of Escrow Funds (Execute a copy of each request.)	(EC)
HUD-2456	Escrow Deposit Agreement (if any)	(EC)
FHA-2455	Request for Endorsement of Credit Instrument Certificate of Mortgagee, Mortgagor and General Contractor (For Insurance Upon Completion only)	(O)
Format	Guarantee Against Latent Defects (Cash Escrow)	(EC)
Format	Letters Assuring Use of Utility Services (Water, Electricity, Sewer, Gas, and Heat)	(EC)
Format	Collateral Agreements (if any)	(EC)
Format	Tax Exemption Letters (if any)	(EC)
HUD-2485	Permission to Occupy – Project Mortgages	(EC)

Format	Municipal Certificate of Occupancy	(EC)
HUD-9839(A,B,C)	Certificate of Management Agent	(O)
HUD-9832	Management Agent Profile	(O)
HUD-92330	Mortgagor's Certificate of Actual Cost	(O)
HUD-92330-A	Contractor's Certificate of Actual Cost	(O)
HUD-92331	Summary of Cost Certification Review, Cost Section	(C)
	HUD-92331-A Cost Certification Review Worksheet, Mortgage Credit Section	(C)
HUD-92580	Maximum Insurable Mortgage	(O)
HUD-2205-A	Mortgagor's Certificate/Actual Cost/Section Section 223(f)	(O)
HUD-92476-A	Escrow Agreement, Additional Contribution by Sponsor	(O)
HUD-92476-A-CA	Escrow Agreement, Additional Contribution by Sponsor	(EC)
HUD-92476.1	Escrow Agreement for Unpaid Construction Costs	(EC)
Format	Section 8 Assistance HAP Contract Documents (If any)	(C)
HUD-92503	Rent Supplement Contract (if any)	(EC)
FHA-1708	Agreement for payment of Real Property by Taxes	(EC)
Format	AIA DOC B108 Standard Form of Agreement Between Owner and Architect for a Federally Funded or Insured Project	(EC)
Format	HUD Addendum to the Owner-Architect Agreement	(EC)
HUD 92531	Housing Consultant's Certificate	(O)
HUD-92531-A-CA	Standard Contract for Housing Consultant Services for Nonprofit Projects Under HUD Programs Exclusive of Section 202	(EC)
HUD-92580	Maximum Insurable Mortgage	(O)
HUD-92531-B	Housing Consultant's Certified Receipt	(O)
Format	Licenses (Section 242, and Elderly)	(EC)
Format	Work Write-up/List of Required Repairs (if repairs after closing.) (223(f))	(O)
Format	Schedule of Values (if repairs after closing) (223(f))	(O)
Format	Progress Schedule (if repairs after closing) (223(f))	(O)

Format	Schedule of Delayed/Interrupted Occupancy (if repairs after closing) (223(f))	(O)
Format	Escrow for Completing Repairs After Closing Completion (if any) (223 (f))	(EC)
Format	Initial Operating Deficit Escrow, if any	(EC)

TITLE SECTION

Format	Title Evidence, as accepted at closing	(DO)
HUD-92457	Surveyor's Report and Certified Property Survey (See Note Section No. 5 below)	(C)
Format	Maintenance Agreement (if any) (For maintenance of facilities shared under common use easements)	(C)
Format	Lease (Ground lease or model lease forms, if any)	(C)
FHA-2070	Lease Addendum for 207 Project	(C)
Format	Land Disposition Contract and Deed (if project is in Urban Renewal Area)	(C)
HUD-27038	Official Receipt/ Federal Housing Administration	(O)

MORTGAGE SECTION

	Mortgage Bond or Note (FHA Form, as finally endorsed)	(C)
	* Mortgage or Deed of Trust (FHA Form, as executed)	(C)
Format	Modification Agreement (if any)	(C)
Format	List of Major Movable Equipment included in the Mortgage or Chattel Mortgage	(C)
Format	Chattel Mortgage, (or)	(O)
Format`	Security Agreement and Financing Statement, (or)	(O)
Format	Mortgagee's Attorney's Opinion that Neither is Necessary	(O)
HUD-92466	* Regulatory Agreement	(O)
FHA-1710	Residual Receipts Note (Nonprofit Mortgagors)	(C)
FHA-1712	Residual Receipts Note/LTD Distribution Mortgagors	(C)
HUD-92223	Promissory Note	(C)
HUD-92433	Mortgagor’s Certificate	(O)
HUD-2434	Mortgagee’s Certificate	(O)
HUD-92447	Property Insurance Requirements	(EC)
HUD-92329	Property Insurance Schedule – Insurable Values for Property Insurance Coverage	(C)
Format	Comprehensive Attorney’s Opinion	(O)

CORPORATE SECTION

Format	Corporate Charter or Partnership Agreement	(CC)
Format	Certificate of Incorporation of Mortgagor	(CC)
Format	Certificate of Domestication (if any)	(CC)
Format	By-Laws (if Mortgagor is a Corporation)	(CC)
Format	Stock Subscription Agreements	(CC)
Format	Minutes of Meetings, Resolutions, Organization, etc., of Directors and Shareholders of Mortgagor	(CC)
FHA-2478	Mortgagor's Oath	(O)
FHA-3281	Approved Management Contract, (or)	(C)
Format	Approval of Management Arrangements	(C)
Format	Declaration (Coops)	(C)
Format	Cooperative Informational, Organizational and Sales Documents (Coops)	(C)
Format	Verification, Non Identity-of-Interest between Mortgagee & Mortgagor	(O)

FISCAL SECTION

HUD-2409	Amortization Schedule Request/MF Mortgages	(O)
FHA-3307	Computation of Advance Amortization	(O)
FHA-3635	Closing Fiscal Examination Work Sheet	(O)
FHA-2283	Financial Requirements for Closing (Final employed in closing)	(C)
Format	Operating Budgets	(C)
	* Reservation of Contract Authority (Subsidized Programs)	(C)
Format	Effective Date of Interest Reduction Contract (Section 236)	(C)
Format	Reservation of Contract Authority (Subsidized Programs)	(EC)
HUD-92451	Financial Record of Mortgage Loan Transaction	(O)
HUD-92410	Statement of Profit and Loss	(C)
HUD-2328	Contractor's and/or Mortgagor's Cost Breakdown (Schedule of values)	(EC)
Format	Secondary Financing Format	(O)
Format	Mortgagor’s Financing Plan	(O)
Format	Verification of existing indebtedness or purchase agreement	(O)
HUD-213	Sales Projection	(O)

CLOSING SECTION

FHA-2400	Certificate of Closing Attorney/Legal Requirements (Initial and Final)	(O)
Format	FHA closing Receipt (Initial and Final)	(O)
FHA-260	Chronology of Actions (Section 202/ 811)	(O)
HUD-290	Closing Memorandum	(O)
Format	Attendance Lists	(O)
Format	Director's Certification that all Administrative Requirements have been met	(O)

MORTGAGE CREDIT CONTROL FILES

(Left Side of Docket)

Format	Financial Statement/Financial Reports/Balance Sheets/Statement of Income	(C)
Format	Rent Roll (223(f))	(C)
Format	Dun and Bradstreet Reports	(O)
Format	Credit Bureau Reports	(O)
HUD-92417	Personal Financial and Credit Statements	(O)
FHA-20l6F	Supplementary Mortgage Credit Report Analysis of Project Sponsorship	(O)
Format	Accountant's Reports	(O)
Format	Correspondence re: Financial Status of Sponsors, etc.	(C)
Format	Resident Accounts Receivable and Delinquency Analysis Report (223(f))	(O)
Format	Rent Formula for Existing Rental Housing (223(f))	(O)
Format	Replacement Cost Formula (223(f))	(O)
Format	Compute Maximum Amount Permitted to be financed through Promissory Notes in a Refinancing Transaction (223(f))	(O)
Format	Schedule of Washington Docket Contents (Completed, Reviewed and certified by HUD closing attorney) (Top left hand side of file)	(O)

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ATTORNEY'S CERTIFICATION: I, _____, HUD closing attorney for subject project, have reviewed this Washington Docket on _____, and to the best of my knowledge the closing documents therein are complete and accurate. Modifications to the list of documents are entered on the list. Modifications to any forms used are listed on the attached Addendum _____ Addendum _____lists documents that must be included in a supplement (documents for outstanding escrows, etc.).

NOTES:

* **Fill in the appropriate Form number or form suffix requires for specific project because of Section of the Act.**

Note 1. The original of each application filed for a SAMA or Feasibility Letter, or Conditional or Firm Commitment and of related correspondence must be included.

Note 2. A copy of the SAMA or Feasibility Letter or the Commitment must be included in the Washington Docket, along with copies of any and all correspondence evidencing their extension, amendment, termination or reissuance, increase, or transmittal to the mortgagee. If the SAMA/Feasibility Letter or the commitment were hand delivered, the date of such delivery should be included in a memorandum to "Washington Docket".

Note 3. Check to determine that the insured aggregate agrees with the total disbursements revealed in Form HUD-92023.

Note 4. This form must show each disbursement and its date of advance to the borrower.

Note 5. Include Form HUD-92457 and the survey submitted for each of the following steps, as applicable to the project: initial endorsement, request for final advance and final endorsement for projects with insured advances; and endorsement for insurance upon completion projects and existing projects insured pursuant to Section 223(f).

COMPLETION INSTRUCTIONS FOR THE WASHINGTON DOCKET

1. The Hub/Program Center Director is responsible for the Washington Docket's preparation, HUD closing attorney's review, and transmittal to Headquarters within 30 working days of closing.

2. The Hub/Program Center Director's designee for assembling the Washington Docket is responsible for including applicable project documents by the listed categories and sequence.

3. Add/Delete Documents as appropriate to the project due to governing conditions, e.g., applicable Section of the Act, Insured Advances/Insurance Upon Completion Projects, Sureties used, etc.

4. The list is not intended to be totally comprehensive for all programs and specifically does not fully cover the forms and documents used in conjunction with the cooperative, condominium, hospital, group practice facility, Title X land development, military housing, elderly housing, and certain projects involving subsidy programs such as Section 8. These programs often involve similar documents and forms with different numbers, and forms and documents unique to the specific program.

5. Use the initial closing check list (Form FHA-1022) to help identify applicable Washington Docket documents. Do not omit any documents that might assist in the financial audit.

6. Strike from the list any document that is not applicable to the subject project, and list those that are additionally required.

7. Separate the Washington Docket by clearly labeled dividers into the following sections: APPLICATION, CONTACT, TITLE, MORTGAGE, CORPORATE, FISCAL, CLOSING, AND MORTGAGE CREDIT.

8. Include only the indicated document type, i.e., original (O), certified (C), conformed copy (CC), duplicate original (DO), and executed or photo static copy (EC), as identified in the list.

9. The Director of Housing Development and the HUD closing attorney are both responsible for the review, assembly and certification to the completeness of the Washington Docket. Any deviation from the listed requirements must be explained in the certifications.

10. See Section II Paragraph C of the Notice for additional Washington Docket completion and submission instructions.

11. Any deviation from the listed requirements must be explained in the certification.

12. The HUD closing attorney must review and certify that the legal closing documents, i.e. that all documents included in the field legal office closing files are contained in Washington Docket.

Appendix 12

Construction Period
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[redacted]

Appendix	Title
12A	Instructions for Approval of Initial / Interim Advances
12B	Contractor's Monthly Requisition and Related Matters
12C	Amendment to the Construction Contract for Payment for Components Stored Offsite
12D	Problems Before Final Closing

Instructions for Approval of Initial / Interim Advances

12A

A. Approving Initial/Interim Advances

1. Before advancing any insured mortgage proceeds, funds provided by the mortgagor must be disbursed in full for project work, material, and incidental charges and expenses from other available funding sources in the following order:
   a. All funds from the cash escrow established by the mortgagor for: onsite construction, fees, carrying charges, and financing (front money escrow).
   b. Grant/loan proceeds furnished by a national, regional, or local community service organization or a private source.
   c. Grant/loan proceeds furnished by a government agency or instrumentality or low-income housing tax credit syndication proceeds, or historic tax credits syndication proceeds, or new market tax credit proceeds, need not be fully disbursed before the disbursement of mortgage proceeds unless the Hub or Program Center Director has previously approved a pro-rata agreement for governmental source funds and tax credits per 24 CFR 200.54. In the case of mortgage insurance for construction or rehabilitation, (purchase or refinancing) of a multifamily tax credit project, HUD cannot require the escrowing of tax credit equity or any other form of security, such as a letter of credit.
2. The amount approved for a requested item cannot exceed the amount claimed by the mortgagor. Release of the front money cash escrow may not be targeted to the completion of specific on-site improvements.
3. The Lender states on Form HUD-92403 the cumulative total of all advances made to the mortgagor, including the advance under consideration. Reconcile any discrepancies before recommending approval of the advance.
4. Lender-approved disbursement amounts shall not exceed the sum of the amounts approved:
   a. For mortgage insurance,
   b. For funding from the mortgagor's cash escrow; and
   c. For funding from available grant/loan proceeds.
5. Project Completion Funding and Disbursement of Tax Credits at Initial Endorsement

   The Housing and Economic Development Recovery Act of 2008 (HERA) provides that if the project will receive the benefit of equity from the sale of low-income housing tax credits (LIHTC) syndication proceeds, historic tax credits syndication proceeds, or new markets tax credit proceeds, HUD may not require the escrowing of the equity, or accept any form of security in place thereof, such as a letter of credit. Therefore, the mortgagor will deposit with the MAP Lender cash that is sufficient, when added to the proceeds of the insured mortgage, to assure completion of the project and to pay the initial service charge, carrying charges, and legal and organizational expenses incident to the construction of the project. The Lender

may accept a lesser cash deposit or an alternative to a cash deposit, where the required funding is to be provided by a grant or loan from a Federal, State or local government agency or instrumentality.

a. The mortgagee should have provided a disbursement schedule as a special condition to the firm commitment of the remaining outlay of tax credits increments to HUD or provided with the Financial Record of Mortgage Loan, Form HUD-92451.

b. The mortgagor's initial installment of tax credits is twenty percent (20%) of the amount of tax credits allocated for mortgageable costs. The initial installment must be disbursed on the initial requisition.

c. After the first installment of tax credit equity is disbursed at Initial Endorsement, the subsequent contributions should be made at a time and in a manner during construction to ensure that the statutory limitations based on actual costs for the applicable FHA mortgage program are maintained during construction. To maintain the appropriate balance of tax credit equity and mortgage loan proceeds, at each infusion of equity, the equity may need to be utilized before the next disbursement of mortgage loan proceeds.

d. Creation of the disbursement schedule for subsequent contributions is developed between the mortgagor and the Lender. So HUD is aware that there may be tax credit equity pay-ins related to required reserve capitalization and/or Developer's fee scheduled subsequent to construction completion and the achievement of certain investor tax-related benchmarks established per the partnership or operating agreement controlling the mortgagor entity.

B. Architect's Fees

1. The Architect's cash fee is in AIA Document B108, Standard Form of Agreement Between Owner and Architect for a Federally Funded or Federally Insured Project.

2. If there is one agreement for both design and supervisory services, a specific dollar amount must be indicated for each service.

3. There may be separate agreements for design and for supervisory services.

4. The Architect's design cash fee may be released with the initial advance.

5. Design services provided by others as detailed in the B108 must be supported by contracts approved by HUD during commitment processing before any funds may be advanced.

6. The Mortgagor's and Architect's Certificate, Form HUD-92403.01, must accompany any request or partial request for advance of the design fee.

7. The Architect's supervisory cash fee is advanced based on a percentage of completion method. The maximum amount that may be approved is computed by multiplying the Architect's supervisory cash fee by the percentage of work completed and approved on Form HUD-92448, then deducting the total of installments previously paid.

8. There is no "holdback" applied to the disbursements approved from the Architect's Cash Fee.

C. For Insurance of Advances, the Carrying Charges, Financing, Legal, and Audit Expense must not exceed their allocations in the Building Loan Agreement. Approve items due or already

paid by the mortgagor which are supported by bills or paid receipts. Do not approve costs for interest, taxes and insurance incurred during early start period.

Note: At cost certification, certify to the actual cost without regard to release limitations imposed by the Building Loan Agreement during the Construction period.

1. Interest is to be advanced only when and as earned. The Lender must specify on Form HUD-92403, the period(s) for which interest is requested and the amount for each period.
   a. At initial closing, verify as to whether a 360 or 365-day (or 366, if leap year) factor is to be used in calculating interest. Check each interest request for accuracy based on the factor indicated, and the annual interest rate approved at initial endorsement.
   b. The Lender is prohibited from drawing down interest and refunding a portion of the money to the mortgagor. Such practice constitutes a kickback and is not acceptable to HUD and will be treated as a direct mortgage reduction.
2. Taxes. In approving amounts for this line item:
   a. Do not allow amounts which accrued before initial endorsement.
   b. Approve invoices which are payable during construction, even if a portion of the billing period will be after an allowable cutoff date. Necessary adjustments will be made at the time of cost certification.
3. Insurance. Allow amounts for fire, windstorm, extended coverage, liability, and other risk insurance customarily insured against in the community.
   a. Do not allow amounts which accrued before initial endorsement.
   b. Do not approve invoices/receipts for workmen's compensation and/or public liability insurance which are included in the cost estimate.
4. Mortgage Insurance Premium may not exceed the amount due for 1 year.
5. Initial service charge and permanent lender fees are limited to:
   a. The actual amount paid or the amount stipulated in the Mortgagee's Certificate, Form HUD-2434, whichever is less.
   b. The initial service fee cannot exceed 2 percent.
   c. The combined amount may not exceed 3.5 percent of the mortgage.

      NOTE: If the 3.5 percent included in processing exceeds the financing fee charged by the mortgagee, identify the excess as restricted funds. For bond financed projects it is capped at 5.5 percent. Amounts in excess of 5.5 percent are not mortgageable.
6. Legal fees may be allowed for:
   a. Mortgagee's Counsel to create the mortgagor entity; however, do not allow the cost of legal services to create tax shelters, trusts, etc.
   b. Costs associated with a counsel's review of initial and final closing documents.
   c. Normal interim activities in creating a project.
   d. Documented costs for items in paragraphs 6.a, b, and c above which are due and

payable before or at final closing may be approved in the initial advance, provided the limitation in paragraph 6.e below is not exceeded.

e. Seventy-five percent may be disbursed at initial closing or during construction. The remaining 25 percent may not be released before final endorsement.

NOTE: Do not allow legal expenses of the MAP Lender or legal services connected with land acquisition, title and recording charges and/or obtaining zoning as they are reflected in the land value. Amounts included in Form HUD-92264 for legal and audit expenses are not blanket allowances, but ordinarily set an upper limit on allowable amounts. Non-typical fees must be borne by the mortgagor, unless in an exceptionally complex case, a higher fee is proven by the mortgagor to be necessary and reasonable. Detailed invoices and/or other documentation is required as to the reasonableness, purpose, necessity, and proper classification of all items in the category.

7. Organizational Fees:

a. The amount included in the replacement cost estimate for organizational fees is an allowance to reimburse the mortgagor for costs incurred to:

(1) Initiate a project;

(2) Organize the mortgagor entity;

(3) Organize its planning, financing and construction, and

(4) Control and manage construction through endorsement

(5) Third Party costs (Appraiser etc.)

b. Release based upon the following:

(1) Disburse 65 percent at initial closing.

(2) Disburse 15 percent during construction based upon a percentage of completion.

(3) Disburse the remaining 20 percent at final endorsement.

Note: Lender's Third Party Costs, reflected in Organization Costs are exempted from the 65% rule. The rule only applies to the mortgagor's organizational costs.

c. This allowance may not be used to subordinate the cash requirements for closing.

d. At cost certification allow only the amount included in Section G of Form HUD-92264 for organizational fees, unless fully supporting documentation is submitted by the mortgagor which justifies the need for and reasonableness of the additional expenditure. Any costs incurred in excess of this allowance are not eligible for recognition in processing a mortgage increase or the equity computation on Form HUD-2580, Maximum Insurable Mortgage.

8. Audit fees associated with obtaining an accountant's opinion of the mortgagor's cost certification cannot be advanced until final endorsement.

9. Title and Recording. Approve amounts typically incurred for:

a. Title search and policy at the time of initial endorsement;

b. Recording fees at initial endorsement;

c. Mortgage and stamp taxes;

d. Survey recording fees;

e. Updating title policy during construction;

f. Final title policy and recording charges; and

g. Legal fees incurred with any of the above.

** Do not fully disburse these funds at initial endorsement. Ensure that sufficient funds are maintained in the account to cover title and recording costs required at final endorsement. This may require the approval of an amount less than that requested in the initial draw.

** Do not disburse funds for title and recording cost associated with acquisition of the land or property.

** Legal, organizational, title, recording costs and taxes incurred in connection with the site purchase may be added to the cost of the land in establishing the latest arms' length purchase price.

10. Developer's fee is provided in the estimated replacement cost of Sections 220, 221, 231 projects involving nonprofit mortgagors. Part or the entire fee may be used to pay for transactional costs associated with developing the project including but not limited to:

    a. Reduction of the estimated closing costs of the project;

    b. Staff salaries;

    c. Nonprofit working capital deposit;

    d. Relocation expenses;

    e. Operating deficit escrow;

    f. Financing fees over and above the 3.5 percent included in the estimated replacement cost of the project;

    g. Environment studies; and

    h. Housing Consultant services provided by either in-house staff or contractor.

11. Pre-marketing Allowance. A pre-marketing allowance computed as $1,500 per unit is included in the replacement cost. This pre-marketing budget allows the mortgagor to pay rent, hire marketing staff, and buy promotional services, consultants, and supplies. To obtain release of the pre-marketing funds, the mortgagor must submit a schedule of marketing and lease-up activities prior to initial endorsement. HUD must approve the pre-marketing schedule including the start of lease-up activities.

12. Tap fees, soil testing and other fees. Approved disbursement must be fully supported and is not to exceed the amount estimated in the general contractor's or mortgagor's list of other fees for requested items. Approve disbursement only for items actually due.

13. The contingency reserve is included in the replacement cost of substantial rehabilitation projects.

    a. Use the contingency reserve for:

(1) Unforeseen costs of necessary changes approved by the HUD Office.

(2) Unanticipated soft costs associated with extension of time change orders approved by the HUD Office.

b. Changes classified as betterments by Architectural and Cost staff is ineligible for funding.

14. Third-Party Lender Expenses: Fees to be paid for third-party review costs of the Lender including but not limited to Architectural reviews, Cost reviews, appraisals, and market studies.

15. At initial endorsement, HUD fees for examination and inspection.

16. Sums allocated to acquisition cost of land or existing building.

D. Allocation of Cash Available to the Mortgagor:

1. Allocation of cash available to the mortgagor listed on line 42 of Form HUD-2283, Financial Requirements for Closing (excess mortgage proceeds) may be allocated to the following items:

a. New Construction.

(1) Land value equity can be applied to fund operating deficit or working capital escrows, or other cash requirements at initial endorsement. After Initial Endorsement, additional draws from mortgage proceeds associated with the excess land value will only be considered after the designated escrow accounts have been fully exhausted. To HUD's estimate of the "as-is" value of land or the actual latest arms' length purchase price, whichever is less. The latest arms' length purchase price may include the following costs incurred in connection with the site purchase:

(a) Legal fees associated with negotiations for acquisition of land, zoning, and examination of title on the purchase or defense of title after purchase.

(b) Prepaid special assessments.

(c) Interest on bridge loans to purchase property after the date of submission of the initial application for mortgage insurance.

(d) Taxes.

(e) Cost of improvements made to the project site by the sponsor/mortgagor.

(2) Cash escrow to cover offsite construction cost.

(3) Cost of any demolition reflected in the Fair Market Value of Land. Payment is approved as demolition progresses.

(4) Construction and/or permanent loan discounts required to be paid at initial closing.

(5) Cash to cover interest shortfall escrow, working capital deposit(s) (i.e. 2% escrow and 2% construction contingency), initial operating deposit, non-realty items, and any permanent loan discounts not required to be paid at initial closing.

(6) Remaining balance may be used to fund any approved change orders or held until final endorsement.

b. Rehabilitation of Existing Construction.

(1) HUD's estimate of the "as-is" value by market comparison or the mortgagor's acquisition cost/existing indebtedness, whichever is less.

(2) Items a (1) through (6) above.

E. Restricted Excess Mortgage Proceeds:

1. Restricted excess mortgage proceeds are those excess mortgage proceeds determined not to be available to the mortgagor during construction, i.e., difference by which the HUD estimate exceeds contract amounts.

   a. These funds cannot be used to satisfy any escrow requirements and must be held until final endorsement.

   b. Identify these funds in an unused column of Form HUD-92451 as restricted funds.

F. Lender Duties for Processing Form HUD-92403. The Lender must review and approve Form HUD-92403 conducting the following major responsibilities:

1. Reconcile any discrepancies between the cumulative total for all advances, including the advance under consideration, and conclusions reached in the processing before recommending the advance for approval.

   a. Enter any required adjustments in Column B and note, "No Adjustment Necessary, Except as Indicated," or "No Adjustment Necessary," as appropriate.

   b. Enter the approved amount in the "Certificate of Mortgage Insurance" on the face of the form, and where the request is reduced; explain the disallowance on the form's reverse side.

2. Determine monthly that advances are proportionate to construction progress.

   a. Require the Lender's underwriter to advise you where advances for "soft costs", i.e., financing and carrying charges, are in excess of work progress as shown by the most current Progress Schedule accepted by the HUD and the percentage of project completion reflected on Form HUD-92448.

   b. Take action where the mortgage is not in balance due to the fault of the contractor.

3. The amount advanced for construction retainage items must be adjusted for a 10 percent holdback of the construction contact amount from each advance, if the follow conditions are met:

   a. The Contractor has no identity-of-interest with the owner greater than a 5 percent equity interest,

   b. If applicable, prior written consent from the surety company must be attached to the request for release, and

   c. There are no questions regarding the contractor's performance concerning the quality of work, compliance with the contract and any change orders or work in progress.

Assuming these conditions are met, the existing standard of 10% retainage will be required until 50% completion. After that, the requirement will be 5% retainage until 75% completion and 2.5% retainage until the loan reaches final endorsement

4. Secure approval from HUD for any advance requesting release of any portion of the contractor's 10 percent holdback.
5. Maintain a record of approved disbursements on Form HUD-92451, Financial Record of Mortgage Loan Transaction.

G. Certificate of Mortgage Insurance: (Prepare when the advance is eligible for approval.)

1. The approved sum is the total for the Contractor's Requisition and other eligible line items.
2. The total approved for any item must not exceed the amount allocated to the item unless the Lender submits a written request to HUD for permission to reallocate funds between line items.
3. The sum approved for mortgage insurance is the amount approved for advance less any funds remaining in the front money escrow and any grant/loan proceeds.
4. For interim advances, the Lender is to prepare this Certificate and sign for HUD, to increase the amount of mortgage insurance.
5. After signing Form HUD-92403 in the space for the Authorized HUD Official, and signing Form HUD-92448 for the Director of Housing Development, the Lender sends a copy of Forms HUD-92403, HUD-92448, HUD-92451, and supporting documentation to HUD.

H. HUD Monitoring of Interim Draws. HUD mortgage credit staff will monitor interim draws. If a problem is encountered during an interim draw, HUD mortgage credit staff will bring the problem to the Hub Director's attention in order to:

1. Modify the next draw, or
2. Withdraw the Lender's authority to approve advances.

Contractor's Monthly Requisition and Related Matters

12B

A. Contractor's Monthly Requisition must be made on Form HUD-92448. The Contractor's Prevailing Wage Certificate on the form's reverse side must be signed. The HUD Inspector reviews for acceptability. If acceptable, forward to Lender's mortgage credit analyst for further processing.

1. Eligible items for inclusion on Form HUD-92448.

   a. Acceptably completed onsite work, i.e. in full compliance with contract documents;

   b. Materials acceptably stored onsite itemized by quantity and cost with supporting invoices;

   c. Components acceptably stored offsite, where provisions are made at initial closing in accordance with Chapter 12, and requirements of Paragraph B below are met.

   d. The Architect determines amounts due by job site observation of acceptable work. (The HUD Inspector makes the determination if there is no Architect.)

   e. The HUD Inspector:

      (1) Checks the Architect's determination using Form HUD-2328, Schedule of Values, and trade item cost breakdowns (guides) to assure that amounts are reasonable for acceptable work and that funds remain for unacceptable and incomplete work;

      (1) Spot checks the count of stored onsite items, determines that storage is acceptable, and assures that amounts are reasonable for approval;

      (3) Checks the invoice and certificate for stored onsite items, and approves payment after assuring that funds remain for transportation to the site and erection.

2. Ineligible items for inclusion on Form HUD-92448.

   a. Noncompliant work and work supported or dependent upon noncompliant work. Work changes completed in anticipation of future change order approvals are noncompliant work.

b. Additive change orders. Refer all change orders to HUD for processing and payment.

c. Offsite work. See Paragraph C below for the contractor's requisition of payment, and release of funds to the mortgagor for acceptably completed offsite work.

3. Modification of Contractor's Requested Amount.

   Where there is disagreement with the requisition, the HUD inspector may modify the contractor's requested amount by:

   a. Entering trade item modification(s) on Form HUD-92448;

   b. Explaining the modification(s) in the HUD Representative's Trip Report, Form HUD-95379.

   c. Completion of Form HUD-92448, Items (1) through (13) are made by the Lender.

4. Supporting Documentation.

   a. In order to help the HUD Inspector reconcile differences with contractor claims, the contractor will submit receipts, bills of lading for onsite deliveries, billings for onsite work, evidence of onsite payrolls, etc.

   b. Surveys may be submitted with each contractor's requisition for improvements not previously shown on a survey, especially regarding:

      (1) Where the siting of structures or setting of finished floor elevations are questioned;

      (2) Location of materials stored onsite.

   c. A survey is required for the next to last advance.

B. Components Stored Offsite.

1. Eligible Building Components. Only "building components" qualify for insurance of advances when stored offsite.

a. An "eligible building component" is a manufactured or pre-assembled building element which, by reason of bulk, size or weight, vulnerability to weather conditions or lack of space at the site, is impractical to store at the site.

b. Eligible building components comprise, but are not limited to:

(1) Precast concrete floor, wall, and roof panels;

(2) Assembled bath and/or kitchen core units;

(3) Fully fabricated structural steel beams and columns.

c. Items that are not eligible "building components" are (but not limited to): kitchen appliances, carpeting, wood roof trusses, etc.

2. Basic Requirements for insured advances.

a. The Lender must have agreed to the necessary provisions at initial closing. See Chapter 12 Sections 12.5 and 12.20

b. The Construction Contract must include the rider "Amendment to the Construction Contract for Components Stored Offsite." See Forms Appendix.

c. Payments are limited to the invoice value of the components.

d. The contractor and its surety bear full responsibility for fraudulent claims for payment and fraudulent disposition of such payments. Safeguards are to protect against premature payments, against materials that do not meet contract requirements and against losses not covered by insurance.

e. The construction contract must be secured by a 100 percent performance and payment bond.

f. Components must be stored at a location approved by the Lender and HUD.

3. Lender's Responsibilities.

a. File Uniform Commercial Code (UCC)-1, financing statements with the proper office in the proper jurisdiction.

b. Make whatever additional filings are necessary to maintain a first lien on the components until they are incorporated into the building(s).

c. Release the financing statement filings as appropriate.

d. Unconditionally certify by letter to HUD that the security instrument(s) is (are) a "first lien" on the components covered by the instrument(s). The Lender's certification must be supported by an opinion from the Lender's counsel.

e. In the event of default under the mortgage, either assign its security interest to HUD or acquire title through foreclosure to the components intended for use or incorporation into the building(s) and convey title to HUD.

4. General Contractors' Responsibilities.

a. All direct and indirect costs associated with the storage and transportation of components stored offsite;

b. Obtaining a risk of loss insurance policy which covers the components. Evidence of this policy must be submitted to the Lender prior to approval of any advance for components stored offsite;

c. Assurance that there is a valid security agreement that is a first lien on the components.

5. Contractor's Requisition. All requests for payment for components stored offsite must be submitted on Form HUD-92448, Contractor's Requisition, accompanied by the following:

a. A statement from the mortgagor's Architect certifying that:

(1) He/she has visited the storage site and inspected the components for which payment has been requested;

(2) The components are in good condition and they comply with the contract

requirements;

(3) The components are properly stored and protected;

(4) The components are segregated, in an easily identified manner from other materials stored at the same site and are marked for identification;

b. A bill of sale accompanied by an itemized invoice transferring title of the components to the mortgagor;

c. A copy of the security agreement provided to the mortgagee by the mortgagor;

d. A copy of the financing statement or statements filed by the Lender in accordance with the Uniform Commercial Code;

e. A warrantee from the Lender that the security instruments represent a first lien on the building components;

f. An opinion from the Lender's attorney that he/she has reviewed the security agreement and associated documents relative to the building components and that the security agreement creates a valid security interest in the collateral and that when the financing statement or statements is (are) duly filed, the secured party will have a first lien.

C. Offsite Construction. Separate from work done under the Construction Contract for the project. Where offsite work is completed by the mortgagor, rather than by a municipality or utility company, a separate construction contract is required, even if completed by the project contractor. Offsite work must also be funded from sources outside the mortgage, except that an escrow for its completion may be funded from available excess mortgage proceeds.

1. Completion Monitoring is performed by the HUD inspector and reported on the Trip Report, Form HUD-95379. See HUD Procedures.

2. Contractor's Requisition is by letter to the mortgagor. Do not use Form HUD-92448 to reflect the value of acceptably completed offsite work, even if completed by the project contractor. Request for Approval of Advance of Escrowed Funds, Form HUD-92464, is used.

3. Construction Changes for offsite work must be requested by letter. Form HUD-92437, Request for Construction Changes, may be used as a guide, but the form itself must not be used for offsite change orders.

Amendment to the Construction Contract for Payment for Components Stored Offsite

12C

A. The undersigned as Contractor and as Owner will abide by the following conditions to induce the Commissioner to release mortgage proceeds for the payment of components stored offsite:

1. The components stored offsite that will be recognized for payment under Article 5 of the contract are those listed and approved by HUD as an appendix to the Contractor's and/or Mortgagor's Cost Breakdown, Form HUD-2328, attached to the Contract as Exhibit "A". The appendix must provide an inventory of the "stored components" and a breakdown of the line item of which the stored components are a part. The breakdown must state:

   a. Cost of Components (Invoice Value),

   b. Cost of transportation form the offsite storage location to the construction site,

   c. Cost of Installation, and

   d. Costs of any other items included in the line item.

2. The Contractor is responsible for:

   a. All direct and indirect costs associated with the storage and transportation of components stored offsite.

   b. Obtaining a risk of loss insurance policy which covers the components during storage, in transit and until installed at the project site. The policy must name the Mortgagor, the Mortgagee and the Commissioner as their interest may appear. Evidence of the existence of this insurance must be submitted to HUD prior to the approval of any advance for components stored offsite.

   c. Assuring to the satisfaction of HUD proper identification and segregation of components while in storage and protection of components while in storage and transportation.

   d. Securing from the mortgagor or mortgagee all necessary security agreements, copies of financing statement, and documentation pertaining to first lien warranties, and

submitting them with the request for payment.

e. Providing corporate surety bonds for on-site improvements on Form HUD-92452M for payment and performance bonds, each equaling 100 percent of the HUD estimate of construction or rehabilitation cost.

3. All requests for payment for components stored offsite must be submitted by the Contractor on Form HUD-92448, Contractor's Requisition, accompanied by the following:

   a. A statement from the Architect certifying that:

      (1) He/she has visited the storage site and inspected the components for which payment has been requested,

      (2) The components are in good condition and they comply with the contract requirement,

      (3) The components are properly stored and protected,

      (4) The components are segregated, in an easily identified manner from other materials stored at the same site and are marked for identification.

   b. A bill of sale accompanied by an itemized invoice transferring title of the components to the mortgagor.

   c. A copy of the security agreement provided to the mortgagee by the mortgagor.

   d. A copy of the financing statement filled by the mortgagee in accordance with the Uniform Commercial Code.

   e. A warranty from the mortgagee that the security instruments requested a first lien on the building components.

   f. An opinion from the mortgagee's attorney that he/she has reviewed the security agreement and associated documents relative to the components for which advance are sought and that the security agreement creates a valid security interest in the collateral and that when the financing statement is duly filed, the secured party will have first lien.

4. Restrictions.

   a. Payments for components stored offsite shall be limited to the cost of components (Invoice Value) identified in the HUD approved appendix to the Contractor's

and/or Mortgagor's Cost Breakdown, Form HUD-2328, attached to the Contract as Exhibit "A," and shall be subject to a 10 percent holdback.

b. In no case shall a payment be approved for components stored offsite to a contractor whose performance, in the judgment of the Hub/PC Manager, is marked by serious deviations from the contract documents.

c. At no time may the outstanding amount of insured advances for components stored offsite exceed 50 percent of the total estimated construction costs a specified in the construction contract.

d. The minimum amount for any single advance is $10,000.

OWNER	CONTRACTOR
_____	_____
_____	_____
DATE: _____	DATE: _____

Problems Before Final Closing

12D

A. General.

1. Additional attention must be given to projects that are experiencing difficulties that may lead to default before reaching final closing. Diagnose problems and take immediate measures during critical periods of project construction to avoid foreclosure or assignment, and to avoid serious hardship to mortgagors, contractors and mortgagees.
2. Prompt action must be taken to correct problems as they arise. Where requested relief cannot be granted for statutory, regulatory or administrative reasons. However, a prompt and final disapproval must be given.

B. Problems leading to default include:

1. Construction problems due to:
   a. Work stoppage,
   b. Contractor abandonment of job,
   c. A change in the contractor, owner or architect during construction,
   d. Construction defects untreated for 30 days, and
   e. Extended periods of bad weather, strikes, etc.
2. Financing problems due to:
   a. Contractor's inability to complete because of under financing.
   b. Overruns in carrying charges due to circumstances beyond the contractor's and mortgagor's control.
   c. Overruns in construction hard costs caused by:
      (1) Mandatory changes,
      (2) Voluntary changes, and
      (3) Price escalation.
3. Inadequate income due to:
   a. Underestimated operating expenses,
   b. Overestimated rents and long-term occupancy levels, and
   c. Inadequate or lack of operating deficit.

C. Defaults during construction. HUD staff will consider alternative measures that can be offered to avoid foreclosure and hardship to all concerned parties regardless of the cause.

1. Request field counsel to provide legal guidance and participate in meetings to discuss

the consequences of default and possible preventive measures.

2. Telephone Lender.
   a. Speak to a responsible official and obtain an opinion on the cause of default, methods of cure and probability of cure.
   b. Advise the Lender:
      (1) To preserve its rights against the surety by giving prompt oral and written notification of the contractor's lack of performance or default, and by demanding performance under the contract of surety (see Paragraph 3. below), and
      (2) To consult with its attorney and to secure HUD approval before entering into any formal or informal agreement with the surety.
3. Notification of Surety. Lender must send a notice to the bonding company with a copy to the general contractor for all conditions affecting the bonding company's interests. The notice should be sent to the bonding company's principal office, and its regional or branch office, attention: Claims Department.
   a. Conditions requiring notification include:
      (1) A sustained work stoppage,
      (2) Nonpayment of subcontractors, suppliers, workmen, etc., and
      (3) Failure to maintain satisfactory progress.
   b. Conditions that require obtaining surety's approval in advance include:
      (1) Approving a change order or aggregate of change orders that exceed 10 percent of the contract price, and
      (2) Extension of the bond by surety where there is a compelling reason why the contractor cannot remedy a latent defect before the bond's expiration date.
   c. The mortgagor is responsible for requesting surety's performance, the Lender must act to protect its and HUD's interests, and HUD must take the final action to protect its interests under conditions in paragraph a. above.
4. Advise the mortgagor of the contractor's violation, and/or lack of performance by the architect or mortgagor, and give 30 days for correction.
5. Assess the situation by considering:
   a. Percentage of construction complete,
   b. Occupancy (including current estimates of income, expenses and occupancy projections),
   c. Type of assurance of completion (bonds, cash escrow),
   d. Status of escrow deposits,
   e. Un-drawn amount of letters of credit (including working capital), and

f. Any other pertinent information.

6. HUD staff should meet to assess available options and prepare a position to present to interested parties. The meeting should include the Hub Director, Field Counsel, and a representative from Asset Management. Separate meetings by staff with one or more of the non-HUD parties may be helpful before holding a general meeting with all interested parties.

7. Convene a general meeting of all interested parties with either a direct or indirect interest in the project to explain the consequences of default. Hold such meetings even where there is no possibility of HUD granting a mortgage increase or other form of relief.

   a. Emphasize that all non-HUD participants must make a meaningful contribution before HUD will assume any additional risk. Such contributions include:

      (1) Infusion of new capital through adding partners, syndication or other investments, and/or

      (2) Concessions by the Lender to avoid a loss (e.g., deferral or forgiveness of interest, taking a partial assignment of the partnership interest, etc.).

   b. State firmly and unequivocally that the non-HUD parties must work out the remedy if the default is to be cured.

   c. Clarify that unless a written firm proposal for a workout is developed; assignment or foreclosure of the mortgage will be the consequence.

   d. Address the remedies covered in paragraph D below, as appropriate.

8. Extension of Lender's election period to assign a loan for insurance benefits should not be granted where a workout proposal is not developed. Thirty days should be the maximum extension in most cases.

D. Remedies to avoid/cure defaults.

1. Call on the Bonding Company to perform, where applicable.

   a. Request field counsel to communicate with surety where it fails to perform to terms of the bond, and

   b. Where surety refuses to honor its obligations after communications by field counsel, request the Department of Treasury to initiate procedures for removal of the surety from the Treasury Circular 570. List the surety, contractor, and project; describe the particulars, including nature of the problem, length of delays and actions taken by mortgagor, mortgagee and HUD to secure surety's performance; and attach a copy of the bond(s). Mail to:

U.S. Department of Treasury
Surety Bond Branch
Financial Management Service
Washington, D.C. 20227

c. Distribute copies of the letter to the Washington Docket, Field Office Docket and Director, Office of Business Products.

2. Lender or Title Company control payments through issuance of two- or three-party checks to assure that disbursed mortgage proceeds are applied for the intended purpose and not diverted to other uses.

   a. All money drawn for construction must actually be paid to subcontractors, suppliers, and workers on the job.

   b. Money drawn for specified purposes, e.g., architect's fees, insurance premiums, taxes, etc., must not be diverted to other uses.

3. Transfer construction funds to soft cost expenses, i.e., keep the mortgage in balance. The liquidated damages clause in the construction contract provides a source of funds for overruns in interest, taxes, MIP and insurance (soft costs) that are due to construction delays which are the general contractor's fault.

   a. Authorize the transfer of funds from the construction contract for payment of soft cost overruns, where it becomes apparent that the scheduled date for completion cannot be met due to the fault of the contractor. The amount of transferred funds must be reflected on subsequent Forms HUD-92448, as a decrease to item 7, Sum of Cost Breakdown Items Plus Inventories of Materials.

      (1) The transfer of funds will get the attention of the contractor, surety (if any), mortgagor and mortgagee, as well as address any financial necessity.

      (2) Notify the contractor, surety (if any), mortgagor and mortgagee by certified mail of the amount and the reason for the transfer.

      (3) Require written acknowledgement of the notification from the mortgagee and surety, if any.

   b. Computation for funds transfer from the construction budget. When the amount originally allocated to interest on Form HUD-92451, Financial Record of Mortgage Loan Transaction is exhausted or near exhaustion, request the Architect and HUD representative to estimate the earliest date of construction completion. Use this date to:

      (1) Set an assumed completion date.

      (2) Compute the minimum liquidated damages for the period between the completion date specified in the construction contract, as adjusted by approved change orders, and the assumed completion date.

      (3) Transfer the computed amount from Column J, Construction, to Column G, Carrying Charges and Financing, on Form HUD-92451.

         (a) Allocate full amount to interest, initially.

         (b) Only use funds for MIP, taxes and insurance after funds for these line items, and the working capital escrow have been exhausted.

4. Use of contractor's holdback, subject to provisions of paragraph 2 above.
5. Infusion of new money. See Paragraph C.7.a above.
6. Release assurance of completion cash escrow where used in place of a performance and completion bond for the construction contract.
   a. The Hub Director may authorize such release, where:
      (1) The project is nearly complete,
      (2) Project completion and final closing may not be attainable with the remaining mortgage proceeds alone or in combination with the mortgagor's other available assets, and
      (3) Release of the funds will offer an excellent chance for project completion and final closing with clear title.
   b. The entire escrow may be released under such circumstances except for 2-1/2 percent of the contract, which amount is needed to fund the latent defects escrow, subject to:
      (1) The Lender must take steps to assure that all required payments by the contractor have been made or will be met to preclude uncovered liens, and
      (2) Disbursement of such funds and mortgagor's additional contributions must be under strict control of the mortgagee or a title company.
   c. Distribute the Hub Director's written authorization for release of the funds as follows: original to the Washington Docket with copies to the Field Office Docket, Closing Attorney, and Mortgage Credit Control File.
7. Deferment of principal payments where the project is complete and ready for occupancy but cannot go to final closing.
8. Mortgage increase may be provided as discussed in MAP Chapter 13 Section 13.22, where economically feasible. Where the contractor is changed because the original contractor becomes bankrupt, abandons the job, or the contract is terminated due to inadequate contractor performance, any mortgage increase must also be processed in accordance with the following:
   a. Reprocess the project.
      (1) Use rents, expenses, and occupancy ratios current as of the date of reprocessing.
      (2) Take into account the new builder's cost to complete, amounts expended to date, and any increase in carrying charges, financing, etc., due to increased mortgage amount and/or extra construction time over the original estimate.
   b. Mortgage increase conditions.
      (1) The mortgagor provides any required front money.
      (2) Any recovery from the original contractor or surety must be applied first to

reduction of the mortgage on a mandatory basis,

(3) The balance of the net recovery after legal expense, if any, may be used to indemnify the mortgagor, Lender, and others, and

(4) A legal document providing for paragraphs (2) and (3) above must be included as a rider to the Regulatory Agreement and Mortgagee's Certificate at final closing, where such recovery has not been made before and considered in the cost certification.

9. Reanalyze the Cost Certification for inclusion of all allowable costs where final closing has not occurred.

10. Working capital deposit balance.

11. A Section 223(d) Operating Loss Loan where eligible.

E. Default report before final closing, Form HUD-58047. Report monthly on the default and describe the plan for curing it.

1. If default cannot be promptly cured, provide a current estimate of income, expenses and occupancy projections.

2. Report distribution:

a. Director, Office of Multifamily Development, and Director, Office of Asset Management and Office of Quality Assurance, within two weeks of default.

b. Asset Management staff for use with the Multifamily Default Status Report, Form HUD-92426.

F. Decision to foreclose where the contractor becomes bankrupt, abandons the job or the contractor is terminated due to inadequate contractor performance. Encourage the Lender to consider foreclosure and tender of the unfinished property to HUD, where the Hub Director agrees in writing that it would be advantageous to the insurance fund, e.g., instances where interruption of construction occurs at an early stage and market and/or economic conditions have worsened to preclude attaining project viability. Consider surety's position in reaching this determination.

1. Lender tenders unfinished property. Where the Hub Director agrees in writing that accepting conveyance of such unfinished property would be more advantage to the insurance fund than pursuing project completion:

a. Promptly convey the decision to all interested parties.

b. Request field counsel to maintain close communication with the Lender’s and mortgagor's counsel and seek advice from the Office of General Counsel as necessary.

2. Estimate completion cost for the unfinished project to support a subsequent damages claim against the surety for damages due to contractor's failure to perform.

3. Document distribution. Original documents, including the Hub Director's authorization to accept the unfinished project, in the Washington Docket with one copy to the Field

Office Docket, Field Counsel and Mortgage Credit Control File.

G. Recovery of mortgage proceeds. In the event of a mortgage insurance claim before final closing instruct the Lender's to establish communications with the Office of the FHA Comptroller regarding the surcharge of insurance benefits.

H. Tax-exempt bond funded project default before final closing. See MAP Chapter 11 for additional information and riders included in the Note and Lender's Certificate in regards to a default.

1. Prepayment lock-out and/or penalty override. Consider exercising HUD authority to override Lender's prepayment lock-out and/or penalty provisions only where:

   a. The project mortgagor has defaulted and HUD has received notice of such default, in accordance with 24 CFR Section 207.256,

   b. HUD determines that the project is experiencing a net income deficiency that is attributable to more than management inadequacy or lack of owner interest, and that the deficiency's magnitude leaves the mortgagor unable to make required debt service payments, pay all project operating expenses and fund all required HUD reserves,

   c. HUD finds that there is a reasonable likelihood that the mortgagor can arrange to refinance the defaulted loan at a lower interest rate or otherwise reduce the debt service payments through partial prepayment, and

   d. HUD determines that refinancing the defaulted loan at a lower rate or partial prepayment is necessary to restore the project to a financially viable condition and to avoid an insurance claim.

2. Deadline extension for filing claim intentions. Lender must request a three-month extension of the election notice filing deadline in the event of a default within the term of the prepayment lock-out and/or penalty. See MAP Chapter 11 and the Lender's Certificate.

   a. Analyze the project's financial condition and assess the feasibility of arranging a successful refinancing.

   b. Recommend that the Hub Director grant the 3-month extension or a shorter extension of the election notice filing deadline, based upon positive conclusions reached by the analysis in paragraph a. above.

   c. Do not consider additional extensions of the election notice filing deadline, unless specifically requested by the Lender.

I. Grant/loan project with a pro rata disbursement agreement that defaults before completion of construction. The governmental entity must disburse the remaining funds where the request for funds remains in the same ratio as previously authorized.

Appendix 13

Cost Certification

Table of Contents

Specimen Letters

	Title
13A	Specimen Letter - Agreement Authorization Reopening of Mortgage Transaction
13B	Agreement Authorizing Deferment of Principal Payments for Level Annuity Monthly Payment

Specimen Letter - Agreement Authorization Reopening of Mortgage Transaction

13A

(Insert Date)
(Insert Mortgagee's Name and Address)
(Insert Project Number)

Madam/Gentlemen:

We have favorably considered your request to reopen this mortgage transaction to increase the maximum insurable mortgage amount. An increase of $_____ is approved making the new maximum mortgage amount $_____. This increase will be insured pursuant to Section _____ of the National Housing Act, and Regulations there under applicable to the original mortgage, provided all legal instruments are modified in a manner satisfactory to the HUD closing attorney assigned to the case. It is understood that no portion of this increase will become available before final closing.

(Insert the amount of additional fees required and the time of payment thereof in accordance with appropriate Regulations.)

Please signify your acceptance of this agreement to modify by signing all five (5) copies of this letter and returning three (3) of them promptly to *(Insert name and address of the Director, Office of Housing Development)*.

Sincerely,

Accepted HUD By: _____

Name: _____
Title _____

Accepted Mortgagee By: _____

Name: _____

Title _____

Agreement Authorizing Deferment of Principal Payments for Level Annuity Monthly Payment

13B

(Insert Date)

(Insert Mortgagee's Name and Address)

(Insert Project Number)

Madam/Gentlemen:

This letter will serve as our approval of the request for a (further*) stay in the commencement of principal payments on the mortgage covering the subject project. In this connection, the following stipulations are pertinent:

1. It is agreed that principal payments shall be (further*) deferred for the period beginning _____ to _____.

2. The Level Annuity Monthly Payment (Principal and Interest) required to amortize the amount of $_____ at _____% in _____ payments from _____ through _____is $_____.

These changes will not affect the eligibility of the mortgage for insurance under the provisions of Section _____ of the National Housing Act, as amended, and applicable FHA Regulations, provided that before final endorsement of the Mortgage Note, the Building Loan Agreement, the Construction Contract and the mortgage instruments are all modified in a manner satisfactory to the Department of Housing and Urban Development's closing attorney assigned to the case.

In the event of a subsequent claim against the mortgage insurance, insurance benefits will be computed on the basis of the date of default as determined under the terms of the modified mortgage. For the purpose of determining such date, all funds collected during the period of the modification agreement and before your election to claim

mortgage insurance benefits will be applied to full monthly installments in the order in which they fall due under the mortgage as modified. The date of default will be the due date of the first installment not fully paid when the funds are so applied.

* Insert when applicable.

Evidence your acceptance of this agreement to modify by signing all five (5) copies of this letter in the space provided and returning three (3) of them to (Insert name and address of the Director, of the Office of Housing).

Sincerely,

Accepted HUD By: _____

Name: _____

Title _____

Accepted Mortgagee By: _____

Name: _____

Title _____

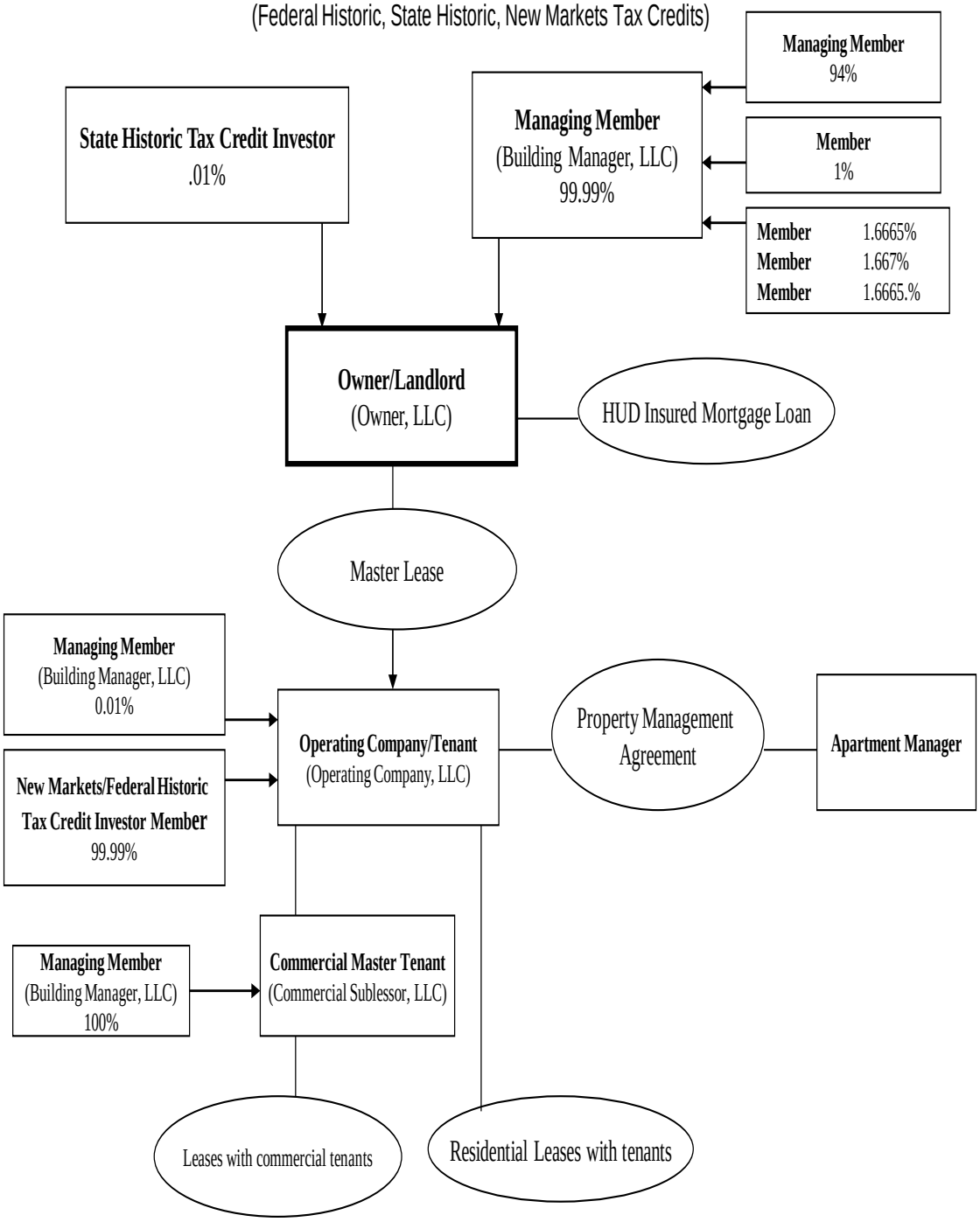
Appendix 16

Sample Master Lease Ownership Structure

Table of Contents

	Title
16A	Sample Master Lease Ownership Structure

Sample Master Lease Ownership Structure

16A

"Sandwich Lease"
ORGANIZATION STRUCTURE/TRANSACTION CHART
(Federal Historic, State Historic, New Markets Tax Credits)