
CHAPTER 5. CONSTRUCTION PERIOD

- 5-1. SCOPE OF THIS CHAPTER. This Chapter covers matters arising in the period between the time an insurance of advances type loan has been initially endorsed and its final endorsement for insurance. It also describes the circumstances under which construction can be commenced prior to initial endorsement. As to insurance upon completion projects, the applicable period is between the commencement of construction and endorsement for insurance.
- 5-2. INTRODUCTION. Following the issuance of a Commitment for Insurance of Advances and initial endorsement of the mortgage note for insurance, the HUD-FHA Director has the responsibility for obtaining the fulfillment of the terms of the commitment and the other documents accepted by HUD at the time of initial endorsement of the loan for insurance, especially with reference to the Construction Contract, FHA Form 2442 or 2442-A and the Building Loan Agreement, FHA Form 2441.
- a. The HUD-FHA Director must also make every effort to make certain that construction of the project progresses according to schedule without unwarranted delays or work stoppage.
 - b. He has the further responsibility for seeing to the proper application and use of construction funds escrowed by the mortgagor, and for the approval of advances of mortgage proceeds to the extent justified by the progress of construction under the terms of the Building Loan Agreement.
 - c. The HUD-FHA Director's responsibility also extends to the approval of construction change orders and the determination of the maximum rental schedule as well as requests for permission to occupy the project.
 - d. The administration and enforcement of labor standards and prevailing wage requirements applying to the construction of the particular project are also the responsibility of HUD-FHA Director.
 - e. Correspondence relating to matters requiring the attention of the Central Office during the period of construction should be addressed to the Office of Underwriting Standards.
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- 5-3. COMMENCEMENT OF CONSTRUCTION PRIOR TO INITIAL ENDORSEMENT. In

insurance of advances cases, construction may commence before formal closing and recordation of the insured mortgage pursuant to FHA Form 3265 with the prior approval of the HUD-FHA Director.

- a. Proposals Meriting Serious Consideration Include those where approaching adverse weather conditions justify an immediate commencement of construction, and where a work backlog in the HUD-FHA office or other factors prevent an expeditious closing. In management type cases, consideration may also be given to those situations where a reasonable number of approved subscribers has been obtained but less than the 90% necessary for closing, and where the commencement of construction prior to closing can reasonably be expected to rapidly bring about the sale of the remaining units and reduce the waiting time of the existing subscribers.
 - b. When, After Analysis and Clearance by Architectural Personnel and the HUD Area Counsel, the HUD-FHA Director is satisfied that such permission will not act to the detriment of the Secretary's interest, approval may be given. The FHA Form 3265 must be jointly executed by the Contractor, Mortgagor and Mortgagee.
- 5-4. CONSTRUCTION FUND OF MORTGAGOR HELD BY MORTGAGEE. The mortgagor may have been required at closing, by commitment provision, to deposit with the mortgagee funds necessary to defray the cost of on-site improvements in excess of mortgage proceeds. The Building Loan Agreement, FHA Form 2441, contains the borrower's agreement * that such funds will be advanced by the lender prior to the advance of any proceeds of the mortgage loan. The Mortgagee's Certificate, FHA Form 3224 in Management Type cases specifies that such funds will be advanced to the mortgagor before any proceeds of the mortgage loan are advanced. In keeping with these requirements the HUD-FHA Director will make certain that full * disbursement of such funds has been made before approving any request for insurance of advances of mortgage proceeds.
- 5-5. APPLICATION FOR INSURANCE OF ADVANCE OF MORTGAGE PROCEEDS, FHA FORM 2403. This is an application for insurance of an advance under the mortgage and is self-explanatory. It must be completed and executed by the mortgagor and the mortgagee, and must be submitted by the mortgagee in triplicate.

- (5-5) a. If the Application is for an Initial Advance of mortgage proceeds, the HUD-FHA Director will determine that all deposited funds held in escrow have been disbursed.

- b. If the Application is for a Second or a Later Advance, the mortgagee must state the cumulative amount of all advances made to the mortgagor, including the advance for which approval is being requested. This total is sometimes at variance with the total amount of advances approved, either because the mortgagee has advanced funds without HUD approval or because the stated total is incorrect. Any such variance must be accounted for and satisfactorily adjusted.
- c. If the Advance to be Insured Includes a Payment to the Architect or a payment on Account of Construction costs, the application must also be executed by the architect. In addition, if the advance includes a payment on construction costs, the application must be accompanied by Contractor's Requisition, FHA Form 2448, and Contractor's Prevailing Wage Certificate, FHA Form 2403-A, completed and executed by the contractor.
- d. Supporting Statement. Except for the first advance of construction funds, FHA Form 2448, Contractor's Requisition, must be supported by a statement on the form reading as follows:

"Date _____ 19 _____

I/We hereby certify that I/we have received payment, in cash of \$ _____ up to the date hereof on the construction contract applicable to this project."

Contractor
(Authorized Signature)

- e. The Amount Cited in the Statement should agree in all cases with the amount entered by the contractor on line (10) in the lower half of the FHA Form 2448, identified as "Less Previous Payments." In any case where the amount in the certificate

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- (5-5) described above is not in agreement with the amount on line (10) of FHA Form 2448, a written report of the discrepancy, together with any explanatory information available, will be made to the Office of Underwriting Standards and no advance will be approved on FHA Form 2403 until written permission is obtained from Washington. (EXCEPTION: Where the difference is minor in amount (ordinarily less than \$2,500.) and can be reconciled by a written explanation from the mortgagee, the advance may be approved prior to sending an account of the difference and a copy of the explanation to Washington.)
- * (5-5) described above is not in agreement with the amount on line (10) of FHA Form 2448, a written report of the discrepancy, together with any explanatory information available, will be made to the Office of Underwriting Standards and no advance will be approved on FHA Form 2403 until written permission is obtained from Washington. (EXCEPTION: Where the difference is minor in amount (ordinarily less than \$2,500.) and can be reconciled by a written explanation from the mortgagee, the advance may be approved prior to sending an account of the difference and a copy of the explanation to Washington.)

- f. The Construction Contract requires a survey showing the location of the improvements constructed on the site. The survey will be prepared by a licensed surveyor and shall be attached to each application for insurance of an advance covering each unit or building not previously located on the survey. After all of the buildings to be constructed are located on the survey, the HUD-FHA Director may dispense with further surveys up to but not including the final advance of mortgage proceeds. (See Chapter 6 of this Handbook.) Upon receipt, the FHA Form 2403 will be referred to the Chief Underwriter (or his Area Office counterpart) for processing in accordance with underwriting procedures. After processing the Chief Underwriter will complete the certificate of mortgage insurance on the form and submit it to the HUD-FHA Director for execution. *
- g. Before Executing the Form, the HUD-FHA Director will determine that the foregoing requirements have been met. If the application is not for a final advance, and if in his opinion the advance is in order, he will execute the certificate of mortgage insurance on all copies and transmit them as follows:
- (1) Original to the mortgagee.
 - (2) One copy to the Washington Docket.
 - (3) One copy to the ADTS/CU for use of Mortgage Credit Section and eventual filing in duplicate docket.
- h. If the Application is for a Final Advance, the HUD-FHA Director will be guided by the instructions contained in Chapter 6, "Final Endorsement" of this Handbook.

- 5-6. ADVANCES TO COVER CARRYING CHARGES, FINANCING EXPENSES, ETC. The Building Loan Agreement, FHA Form 2441, provides for the advance of mortgage funds if available, to the mortgagor for carrying charges, financing expenses, etc. The amounts allocated to each item should equal the funds allocated to the items in the Project Income Analysis and Appraisal, FHA Form 2264-B. The mortgagee should not permit reallocation of these items without the consent of the HUD-FHA Director, nor should the mortgagee advance funds for any one item in excess of the amount allocated to such item in the Building Loan Agreement. A mortgagee may communicate with the HUD-FHA Director regarding expenses for a single item in excess of the allocation or in connection with a reallocation. The HUD-FHA Director will not consent to the advance of the

mortgage money for any single item in excess of the amount allocated for such item unless there is a corresponding reduction in the amount of another item.

5-7. RELEASE OF HOLDBACK OF MORTGAGE PROCEEDS.

- a. In Insurance of Advances Cases, the Building Loan Agreement requires the retention by the mortgagee of 10% of the construction proceeds at the time of each advance. This retention is one of the few sanctions HUD possesses to achieve as early a final closing of a loan as possible. Not until the time of the last advance is the holdback normally released, thus an earlier release of the funds weakens the incentive on the part of the mortgagor and contractor to take the necessary steps to permit a final closing.
- b. There is Only One Absolute Rule to be applied to a request for early release of the holdback--the prior written consent of the surety. With that consent in hand, the main factors the Director should consider are:
 - (1) The percentage of completion at the time of the request.
 - (2) The amount of the holdback.
 - (3) The portion of the holdback requested to be released.
 - (4) The contractor's performance up to the time the request for release is submitted.

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- c. Prior to Completion of 90% of Construction, such a release should be permitted only if the director is of the opinion the failure to do so would probably result in a default of the construction loan. If such release is granted, measures should be taken to make certain that the proceeds are disbursed immediately and principally for the benefit of the subcontractors.
- d. After 90% of the Construction has been completed, a release of up to 50% of the holdback should normally be permitted, provided the mortgagor and contractor are not primarily responsible for conditions causing the request for an early release, and also provided that there has been general compliance with our requirements by the mortgagor and contractor in the construction of the project to that point.
- e. Once there has been Substantial Completion of the project, acceptable cost certification has been filed, and an early

final closing scheduled, the Director may, at his discretion, release 50% or more of the holdback, but in no event the entire amount thereof, bearing in mind that the undisbursed holdback provides a major incentive to the contractor to complete his performance.

5-8. WORKING CAPITAL.

- a. The Working Capital Deposit, required of all mortgagors, which was made at initial closing as a condition of the commitment, is primarily for the purpose of assuring monthly accruals with the mortgagee during the construction period for the second mortgage insurance premium, the real estate taxes due in the year following completion of construction, and the total premiums for permanent property insurance for one year in order that all such items may be paid by the mortgagee when due, as required by the terms of the mortgage. The balance of the deposit is for the purpose of defraying expenses during the opening of the project for occupancy. If a leasehold is involved and the lease provides for the payment of ground rent during the construction period, an amount sufficient to pay such ground rent must be included in the deposit. The portion of the deposit applicable to ground rent shall be released for that purpose only and shall be released upon a showing that ground rent in a specific dollar amount is due and payable.

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- (5-8) b. Control and Disbursement. The working capital deposit, or provisions of the letter of credit in lieu thereof, is under the sole control of the mortgagee and the disbursement of any portion of it is a matter for the discretion of the mortgagee. However, a mortgagee may refer to a Director a request from the mortgagor for release of a portion of the deposit, or a mortgagor may refer such request to a Director. Upon receipt of such request from either a mortgagor or a mortgagee, the HUD-FHA Director will send his reply to the mortgagee with his comments and recommendations. (In case the request is from the mortgagor, a copy of the Director's reply to the mortgagor should also be forwarded to the mortgagee.) In making his comments and recommendations, the Director will be guided by the following:

- (1) The accrual with the mortgagee of amounts sufficient to defray the cost of the second mortgage insurance premium, the real estate taxes due in the first year subsequent to completion, and the permanent property insurance policies is of primary importance to the mortgagee and HUD.
- (2) No part of the deposit is to be used to defray any of

the cost of construction or other expenses incidental to construction.

- (3) Instead, any balance in excess of amounts necessary for the required accruals is for the purpose of defraying opening expenses in the nature of renting and advertising and purchase of equipment and supplies necessary for the opening and operation of the project. The HUD-FHA Director will be careful to avoid recommending premature disbursements and unnecessary and extravagant expenditures.
- (4) In many instances, however, portions of a project may be completed and ready for occupancy before completion of the entire project, and disbursement for reasonable opening expenses for such completed portions of a project may be permitted. But the Director will exercise sound discretion in recommending approval or disapproval of opening expenses in connection with such completed portions of a project in order that the deposit will not be exhausted before completion of the entire project.

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- (5) The HUD-FHA Director will make it clear that his comments are recommendations only and that final action is at the discretion of the mortgagee.
- 5-9. WORKING CAPITAL REQUIREMENTS IN THE COMMITMENT FORMS. The purpose for which disbursements may be made from the Working Capital account vary under the several forms of commitment. Therefore, reference should be made to the commitment form which is applicable in each case.
 - 5-10. DISBURSEMENT OF FUNDS IN EXCESS OF MORTGAGE PROCEEDS. Under the Mortgagee's Certificate, FHA Form 3220, the mortgagee agrees to advance the escrowed "over and above" funds, prior to making any disbursement of mortgage funds. The HUD-FHA Director should satisfy himself that this has been accomplished prior to approving any request for insurance of an advance of mortgage proceeds.
 - 5-11. OTHER GUARANTEES FOR WORKING CAPITAL. In Presale Management Type cases where an "Agreement for Sale of Land and Development of Project" is used the "over and above" costs are normally covered. It should be checked for acceptability.
 - 5-12. PAYMENT FOR OFF-SITE FACILITIES. If an escrow deposit has been made to assure construction of off-site facilities under the provision of Escrow Agreement for Off-Site Facilities, FHA Form 2446, disbursements may be made from this escrow deposit as the

construction of off-site facilities proceeds. These disbursements will be in proportion to the percentage of off-site work completed, less a holdback of 10%. The mortgagor will submit to the depository his request for payment, in quadruplicate, on Request for Approval of Advance of Escrow Funds, FHA Form 2464. The depository will complete its portion of the form and submit it in triplicate to the Director. Upon receipt, the request will be routed to the ADTS/CU for processing in accordance with underwriting procedures. After processing, the Chief Underwriter will complete the form and submit it to the Director.

a. If the Director finds that the Disbursement is in order he will execute the form and distribute it as follows:

- (1) Original to the depository.
- (2) Two copies to the ADTS/CU, (one copy for use of Mortgage Credit Section, and one copy to be filed in the Washington Docket).

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b. If the Director finds that the Disbursement is not in order, the request will be returned to the sponsor accompanied by a letter setting forth the reasons for denying the release of the escrow funds.

5-13. ASSURANCE OF FUNDS TO MEET OPERATING DEFICITS. If, pursuant to the terms of the commitment the sponsors have agreed to deposit, on the estimated date of completion of project construction, certain funds to meet project operating deficits, the Director shall remind the sponsors of this obligation sufficiently in advance of the completion date to permit them time to arrange for the deposit. Conversely, in certain instances, the sponsors may request the Director's permission to be relieved of their obligation to make such a deposit, in which event the Director shall be guided by the provisions of this Handbook.

5-14. OTHER ASSURANCE OF FUNDS TO MEET OPERATING DEFICITS. If an "Agreement for Sale of Land and Development of Project" is used it should be checked for acceptable coverage. In considering any change in drawings and specifications, the HUD-FHA Director must bear in mind that such changes can be accepted only when they provide for equivalents, betterments or changes due to necessity. In determining the acceptability of equivalents, care should be exercised to prevent establishment of a closed specification which is non-competitive and more costly. Construction changes will be processed as follows:

a. Route the Request to the ADTS/CU for processing in accordance with underwriting instructions. He will be responsible for

the completion of HUD-FHA processing on the back of FHA Form 2437 and for its submission to the Director.

- b. The Director should satisfy himself that: (1) FHA Form 2437 has been properly executed; (2) if any agreement has been executed on the part of the mortgagor to increase the amount of the contract, that such agreement was executed pursuant to a resolution adopted by the members; (3) appropriate escrow deposits have been set up as required below; and (4) if the net increase in cost equals or exceeds 10% of the contract price, approval in writing has been obtained from the bonding company.

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- c. Whenever an Acceptable Change Order Indicates an Increase in cost and the mortgagor assumes responsibility for payment, such increase, if in excess of 1% of the original construction contract amounts shall be deposited in escrow with the mortgagee. When the HUD-FHA estimate of increased cost indicates an increase of 2 1/2% or more of the amount of the construction contract, the additional funds must be deposited in escrow with the mortgagees, regardless of whether the cost is to be absorbed by the contractor in whole or in part.
- d. No Construction Change Resulting in Increased Cost may be accepted unless the contractor or the cooperative has agreed to assume the additional cost. The Director should satisfy himself that any substantial changes in constructions, whether resulting in increased or decreased costs, have been clearly explained to the members and have been accepted by them by resolution.
- e. Executed Copies of FHA Form 2437 bearing the approval or disapproval of HUD, shall be distributed as follows: Three (3) copies to the mortgagee (one copy for the mortgagee, one copy for the mortgagor and one copy for the contractor), and three copies to the ADTS/CU (one copy for the use of the Mortgage Credit Section, one copy for use by the HUD-FHA inspector assigned to the project and one copy to be attached to the master set of drawings and specifications).
- 5-15. INCREASE IN INSURED MORTGAGE AMOUNT. Frequently Field Office Directors are called upon to consider mortgagors' request for increase in insured mortgage amounts owing to increased costs associated with approved changes during construction. At the preconstruction conference with parties concerned with the construction of the project, the Field Office Director should not fail to explain that while changes in plans or specifications during construction may involve increased costs and may result in betterments, it will not automatically follow that an increase in

mortgage amount can be allowed. When approving construction changes, the Field office Director will give no explicit or implied assurance that an increase in mortgage amount will be granted. Instead, particular attention should be invited to "Instructions and Conditions of Acceptance" on the reverse side of FHA Form 2437.

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- (5-15) a. Additional Costs Incurred Incidental to Approved Changes. It is expected that additional costs incurred incidental to approved changes in construction will be satisfied with funds other than mortgage proceeds. In some instances, however, circumstances will warrant approval of a request for an increase in the mortgage amount. Such requests should not be considered until construction has been substantially completed.
- b. An Exception to the foregoing is where the request for increase is made by a nonprofit mortgagor for a change which is essential to health, safety or efficient operation. Here, at the time of approval of the change order, the mortgagor and mortgagee should be notified, in writing, whether or not the mortgage increase will be recognized for insurance. Special consideration should be given where the change is made at the request of HUD. As in the case of any increase, the prior approval of the Regional Administrator must be obtained.
- c. Reasons for Increases Before Final Endorsement. There are two main reasons for considering increases before final endorsement: (1) To correct substantial error in the original processing which would otherwise result in serious inequities, or (2) Substantial changes in the approved plans or specifications that have resulted in significant betterments to the mortgage security which can be reflected in increased income expectancy or lower projection of operating expenses.
- d. Since the Terms of the Mortgage are made Firm at Initial Closing, there should be no subsequent increase in the insurable mortgage amount without a consideration running to the Secretary of HUD. Normally no increase will be considered when the amount involved represents less than 2 1/2% of the original mortgage amount.
- e. If Upon Receipt of a Request for an Increase in Mortgage Amount before final endorsement, the Field Office Director's initial reaction is favorable, an evaluation should be made of the cumulative effect of all acceptable change orders. Such request for an increase will be accompanied by the mortgagee's check for \$1.50 per thousand dollars of the amount of the increase requested. FHA Form 2264-A and 2264-B should be drafted informally to reflect such evaluation, following

* which the forms, together with supporting data will be forwarded promptly with written recommendation from the Field Office Director to the Regional Administrator for review and determination. *

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(5-15) f. The Submission will be Reviewed by the regional staff with the same degree of care and completeness as though it were a new case. If need be, a representative of the Regional Office will visit the Field Office to secure clarification firsthand, of any of the underwriting conclusions reached. Upon completion of his review, the Regional Administrator will return the submission to the Field Office Director with a letter approving or disapproving the request. A copy of his letter will be furnished the Office of Underwriting Standards.

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g. If the Decision is to Allow an Increase, the letter will authorize the reopening of the mortgage transaction predicated upon the preparation, execution and distribution of revised FHA Forms 2264-A and 2264-B and the issuance of a letter agreement, in five-copy form to the mortgagee on the prescribed form (See Figure 1) reciting the payment provisions based on the figures which will be furnished on request by the Office of Finance and Accounting on FHA Form 2798-A, Worksheet Request for Revised Payment. The approval of the increase is subject to the payment of an additional commitment fee which, when added to the additional application fee, will total \$3.00 per thousand of the increase approved. In addition, an inspection fee must be paid in an amount of \$5.00 per thousand of the amount of the increase. Upon return by the mortgagee of the letter agreement, endorsed to evidence its acceptance, one copy will be promptly forwarded to the Office of Underwriting Standards. Reopening of the mortgage transaction for the purpose of effecting an increase in mortgage amount will be accomplished with no change in the interest rate or in the amortization plan or in the maturity date of the mortgage.

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CHAPTER 5, FIGURE 1

LETTER AGREEMENT AUTHORIZING REOPENING OF MORTGAGE TRANSACTION

(Insert Date)

(Insert Mortgagee's Name and Address)

(Insert Project No.)

Gentlemen:

This Department has favorably considered the request to reopen this mortgage transaction so as 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 thereunder applicable to the original mortgage, provided all legal instruments are modified in a manner satisfactory to the Department of Housing and Urban Development closing attorney assigned to the case. It is understood that no portion of this increase will become available prior to final closing.

(Insert provision to fully amortize the increase in accordance with the amortization plan as provided in the original mortgage. Also insert provision as to the amount of additional fees required and the time of payment thereof in accordance with appropriate Regulations.)

We ask that you signify your acceptance of this agreement to modify by signing all five copies of this letter and returning three of them promptly to (Insert name and address of appropriate Field Office Director).

Very truly yours,

ACCEPTED _____
(Date)

Secretary
Department of Housing and
Urban Development

(MORTGAGEE)

BY: _____
Authorized Agent

BY: _____

5-16. EXTENSION OF TIME TO COMPLETE CONSTRUCTION.

- a. Whenever Construction of a Project is Behind Schedule, the HUD-FHA Director will ascertain the nature and extent of the delay and will secure from his underwriting staff advice as to when satisfactory completion may be anticipated. When it becomes apparent that construction cannot be completed within the time originally contemplated in the construction contract

and building loan agreement, the HUD-FHA Director, upon appropriate request from the mortgagor, will ascertain whether the mortgagee will consent to an extension of time within which to complete the project. If such consent is forthcoming, it should be supported by the written consent of the surety.

- b. When Agreement is Reached as to the additional time required for the completion of construction, the HUD-FHA Director may approve the extension, provided that the sponsors furnish assurances acceptable to the HUD-FHA Director that any consequent overrun of interest will be paid from sources other than mortgage proceeds. If assurances offered are unsatisfactory, the HUD-FHA Director will so inform the parties interested and send to the Office of Underwriting Standards a summary of all pertinent facts. *

5-17. DEFERMENT OF PRINCIPAL PAYMENTS. If an extension of time within which to complete the construction is granted, in many instances a deferment of commencement of amortization is also requested. In addition, such requests often arise to permit the mortgagor more time within which to obtain substantial occupancy. When a deserving mortgagor demonstrates hardship, and in recognition of it, the mortgagee joins in a request that the mortgage be modified for the purpose of deferring the commencement of amortization, such request will be considered favorably so long as there is a reasonable prospect that by diligent efforts on the part of a competent management, the income from the property can be brought to a sustaining level. If the HUD-FHA Director considers the request to be justified, he may approve it.

5-18. WORK STOPPAGE. Upon being informed by the ADTS/CU or other members of his staff that a work stoppage has occurred on any project being financed with insured advances, the Field Office Director will communicate immediately with the mortgagee, the

mortgagor and the contractor, to determine the cause of the stoppage and to ascertain when resumption of construction is anticipated. The seriousness of a work stoppage should be impressed upon the parties concerned, especially the mortgagee, mindful that a stoppage continuing for a period of 20 days or more gives rise, at its option, to a default under the mortgage. As soon as it becomes evident to the HUD-FHA Director that efforts to obtain resumption of construction are proving ineffectual, and in every instance when a work stoppage has continued for a period of 20 days, he will cite the facts obtaining to the Office of Underwriting Standards, by wire, and request special guidance as to action to be taken to protect the Secretary's interest. *

(NOTE: The above steps will be taken in addition to any steps that may be prescribed under Compliance instructions.)

5-19. PERMISSION TO OCCUPY. At closing, the mortgagor certified in the Mortgagor's Certificate, FHA Form 2433, that it would not permit occupancy of any portion of the project without the consent of HUD-FHA. Since portions of the project may be ready for occupancy before completion of the entire project, it may be necessary that the mortgagor submit more than one request for approval of occupancy.

a. Occupancy Prior to Completion. Although the parties sometimes consider it desirable to permit occupancy only after construction has been completed and final endorsement of the mortgage note has been effected, there are circumstances under which occupancy prior to completion is desirable and advantageous. The HUD-FHA Director may permit same subject to the following requirements:

- (1) Execution of Permission to Occupy, FHA Form 3219, by the mortgagor, contractor, mortgagee and the ADTS/CU, and approved thereof by the HUD-FHA Director.
- (2) Satisfactory evidence has been submitted that public authorities with competent jurisdiction have issued such permits as may be necessary for lawful occupancy of the project, either in whole or for the portion under consideration.

- b. In Management Type Projects, occupancy should be permitted only upon execution of an occupancy agreement (in form approved by HUD) at the established monthly carrying charge figure. It is possible that the amount collected prior to the completion of the project and prior to the date on which amortization begins will result in a surplus in the treasury of the corporation. The manner in which any such excess income is to be disposed of is set forth in Chapter 4 of this Handbook.
- 5-20. TRANSFER OF PHYSICAL ASSETS DURING CONSTRUCTION PERIOD. In view of the more complicated requirements which must be met to accomplish a transfer of physical assets during the construction period, most mortgagors prefer to wait until after closing. However, if circumstances warrant transfer during the construction period, all the regular requirements, as set forth in Reference (7) of the Foreword must be satisfied, in addition to the following

special requirements:

- a. The Consent to the Sale of the Property. The consent to the sale of the property must be obtained from the surety and the mortgagee. It will also be necessary for the seller to specifically assign to the buyer the working capital deposit and all other funds deposited in escrow. The seller must assign and the buyer must assume and accept all of the obligations, rights, title, and interests of the seller to Construction Contract, Building Loan Agreement, Architect's Agreement, Escrow Agreements, Assurance of Completion, and any letter of credit or bond which may support the completion assurance agreements. The buyer must thereafter execute a new Mortgagor's Certificate, Mortgagor's Oath, and an Agreement and Certification.
- b. The Attorney's Opinion Required by Transfer Instructions, FHA Form 2266-A, must also cover the legality of the assumption by the purchaser of the seller's rights and liabilities under the Building Permits, Construction Contract, Building Loan Agreement, Architect's Agreements, Assurances of Completion, any Escrow Agreements, Special Deposits or letters of Credit, and the execution by the purchaser of a Mortgagor's Certificate, Mortgagor's Oath, Agreement and Certification, and any other documents required by HUD, the seller, or the mortgagee to be executed by the purchaser.

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- c. The Normal Presale Requirements (90%) for management type cooperatives must be met as well as the consumer safeguard provisions for Section 213(i) set forth in Reference (1) of the Foreword

5-21. CONSTRUCTION AND CONTRACT REQUIREMENTS.

- a. HUD does not require the construction contract to be on FHA form. The contract, however, must contain the cost certification and labor provisions stated in the commitment.
- b. Construction must not Commence Before (1) issuance of Commitment to Insure Upon Completion, FHA Form 3209, and payment of commitment and inspection fees; (2) the receipt of Labor Standards and Prevailing Wage Requirements; and (3) the execution of Agreement and Certification, FHA Form 3305-A by the mortgagor, mortgagee, and FHA.
- c. After Execution of FHA Form 3305-A, the copies will be distributed as follows: The original to the Washington Docket, Contract Section; one copy to the mortgagor; one copy to the mortgagee; one copy to the closing attorney and one copy to

the Field Office Docket.

- d. Construction Shall Start within the time limits specified in the commitment. During the course of construction, no advance of mortgage proceeds will be insured. However, construction changes may be involved; the mortgagee must be advised of permanent hazard insurance requirements; the mortgagor must request permission for occupancy; the rental schedule must be approved; and management arrangements must be made. With respect to these matters, the Director will be guided by the following;

- (1) Procedures for Construction Changes (FHA Form 2437) will be the same as provided in Reference (8) of the Foreword except that the Director will have no responsibility for determining that funds are available for increased cost or for notifying the surety or indemnitors of changes. If, however, the Director feels that a change will result in increased cost which the mortgagor may not be able to defray, he should call the matter to the attention of the mortgagee, since, at the time of endorsement of the credit instrument, the mortgagor must not have outstanding any obligations in connection with construction other than the insured mortgage; and the mortgagee is interested in having the property free of liens.

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- (5-21) (2) Property Insurance will be required when construction on-site is 80% complete, and in any event prior to endorsement of the credit instrument, the Director will obtain from the ADTS/CU, in quadruplicate, a completed Property Insurance Schedule, FHA Form 2329. The Director will ascertain from the ADTS/CU that the schedule, at that time, correctly shows the insurable value of the completed structures, reflecting any changes in cost occurring after the issuance of the commitment. Property Insurance Requirements, FHA Form 2447, in quadruplicate, will be prepared and routed as follows:
- (a) Date the form as of the date of its preparation.
- (b) Insert in the spaces provided at the top of the form the name and address of the mortgagee; and the project number, name, and location.
- (c) In paragraph 3, in the space provided, insert the date of the applicable FHA Form 2329 shown at the bottom of the form.
- (d) Staple to each copy of the FHA Form 2447 a copy of

the applicable FHA Form 2329. The Director will then execute FHA Form 2447 in the space provided for signature and forward the original and one copy, with attachments, to the mortgagee. The remaining copies, executed, will be filed, one each, in the Washington and duplicate Dockets. In the event of any revision or correspondence regarding FHA Form 2447 and 2329 copies of such revisions or correspondence will be filed in the Washington and duplicate Dockets.

- e. The Mortgagor is Required to request the consent of HUD-FHA before permitting occupancy on FHA Form 2485, Permission to Occupy, in order that there may be ample opportunity to inspect the project prior to occupancy; and in order that the proposed rental schedule may be agreed upon between HUD-FHA and the mortgagor. Since portions of the project may be ready for occupancy before completion of the entire project, it may be necessary for the mortgagor to submit more than one request for permission to occupy. The Director will notify the ADTS/CU of receipt of request for permission to occupy in order that necessary inspections may be made before occupancy. On receipt of advice from the Chief Underwriter that there are

(5-21) no objections to occupancy, the Director may consent to such occupancy on receipt from the mortgagor of evidence that public authorities with jurisdiction have granted required occupancy permits. No occupancy of the project may be permitted prior to the approval of the Director of the Management Agreement between the owner and the agent.

- f. The Management Requirements will be the same as provided in Insurance of Advances Cases.
- g. A Proposed Rental Schedule will be required upon receipt of the first request for permission to occupy. By submission of the rental schedule before the time of first occupancy, it is possible to avoid adjustments at the time of subsequent closing. Procedure with respect to the approval of a rental schedule will be as provided in Reference (8) of the Foreword.