

CHAPTER 6. MORTGAGE CREDIT PROCESSING

- 6-1. INTRODUCTION. Mortgage Credit Processing will begin at the firm commitment stage and involves: credit investigation; analysis of the acceptability of the sponsorship; determining the amount and amortization period of the loan; evaluation of the mortgagor's ability to close the loan transaction, the mortgagor's cost certification and the mortgagor's ability to liquidate the mortgage debt and successfully operate the project. Mortgage Credit procedures and analyses are to be completed in accordance with HUD Handbook 4470.1, Mortgage Credit Analysis for Project Mortgage Insurance, Section 207, except as modified herein.
- 6-2. MORTGAGE AMOUNT. Analysis of the credit risk is premised upon a loan for a definite amount and amortization period subject to the following limitations:
- a. Principal Obligation. The mortgage will involve a principal obligation in an even multiple of 100.
 - b. Amount of Loan in a Purchase Transaction. The subject loan will be the lesser of:
 - (1) An amount not to exceed 85 percent of the Secretary's estimate of value of the project.
 - (2) The maximum per unit limitation for new construction under Section 207 of the Act plus cost not attributable to dwelling space.
 - (3) An amount which entails a debt service not in excess of 85 percent of the net annual income as estimated by the Secretary.
 - (4) Eighty-five percent of the amount required to acquire the property, as determined by the Secretary. For purposes of this section, the cost of acquisition is defined as the sum of the following:
 - (a) Purchase price as indicated in the purchase agreement and determined allowable by the Secretary.
 - (b) The estimate of repair cost, if any, as determined by the Secretary, provided such costs will be borne by the purchaser and are not included in the purchase price.

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- (c) The sum of the amounts attributable to financing, legal, organizational, and title and recording expenses which the mortgagor

is required to pay and which the Secretary determines are reasonable.

- (d) Discounts as determined eligible by the Secretary provided they are paid by the purchaser.
- (e) The amount as determined by the Secretary for the initial deposit to the Reserve Fund for Replacements, provided such deposit will be funded by the purchaser.
- (f) Architect's fees, mechanical engineering fees, and municipal inspection fees, as may be determined eligible by the Secretary.

c. Amount of Loan in a Refinancing Transaction. The subject loan will be the lesser of:

- (1) An amount not to exceed 85 percent of the Secretary's estimate of value of the project.
- (2) The maximum per unit limitation for new construction under Section 207 of the Act plus cost not attributable to dwelling space.
- (3) An amount which entails a debt service not in excess of 85 percent of the net annual income as estimated by the Secretary.
- (4) An amount which equals the greater of the following:
 - (a) 70% of the Secretary's estimate of the value of the project, or
 - (b) The cost to refinance the project. For purposes of this section, the cost to refinance is defined as the sum of the following:
 - 1 The amount required to pay off the existing indebtedness as determined eligible by the Secretary.
 - 2 The amount as determined by the Secretary for the initial deposit to the Reserve Fund for Replacements.

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- (6-2) 3 The sum of the amounts attributable to financing charges, legal and organizational, and title and recording

expenses which the mortgagor is required to pay and which the Secretary determines are reasonable.

- 4 The estimate of repair cost, if any, as determined by the Secretary.
- 5 Discounts as determined eligible by the Secretary.
- 6 Architect's fees, mechanical engineering fees and municipal inspection fees, as may be determined eligible by the Secretary.

* 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.*

d. Determining the Maximum Insurable Mortgage in a Refinancing Transaction.

- (1) For the purpose of determining the maximum insurable mortgage in a refinancing transaction under Section 223(f) of the Act, existing indebtedness is defined to be:
 - (a) The outstanding mortgage(s) incurred in connection with the construction of the project or with capital improvements made to the property as confirmed by the mortgagee, using the pay-off letter which appears in Exhibit V of this Handbook, and other recorded indebtedness such as mechanics' and tax liens. The tax liens must be for a project indebtedness rather than for an indebtedness against the property arising from a personal obligation of the mortgagor.
 - (b) Some unrecorded indebtednesses, such as, delinquent interest, indebtedness incurred in making significant betterments to the property subsequent to the initial completion of the project, prepayment penalties, etc. If the indebtedness is not recorded, the mortgagor must provide the field office with documentation which unquestionably identifies the indebtedness with the project.

- (6-2) (c) The outstanding indebtedness when an open line of credit is used in the construction of a project. In such cases, a cost certification

prepared by a certified public accountant and submitted on Form FHA-2330 and Form FHA-2330A in the manner prescribed in outstanding HUD instructions must accompany the application for insurance. The cost certification shall not be reviewed in the same manner as those submitted under HUD's other insured loans program but shall be accepted as verification of the actual construction costs which will be eligible for re-financing. The lending institution must verify the amount of the outstanding indebtedness on the line of credit and identify that portion which is attributable to the project.

- (2) In some instances, it shall not be appropriate to recognize the total indebtedness in establishing the maximum mortgage amount. For example, if a second trust has been created shortly before the application for mortgage insurance was filed and runs to an identity of interest party, there is a strong presumption that such debt was created merely for the purpose of securing a larger insured loan to enable the owner to recapture equity out of mortgage proceeds. In any such case, the amount of the existing indebtedness shall not include the second trust unless it can be proven that such trust was essential to the project.
- (3) Any recent indebtedness placed against the property whether or not an identity of interest party is involved must be closely investigated. If it appears that any such indebtedness was placed against the project in an effort to increase the mortgage or to circumvent outstanding instructions, then it shall not be considered existing indebtedness for the purpose of determining the maximum insurable mortgage.

e. Amount of Loan in Older, Declining Neighborhoods. The subject loan shall be as follows:

- (1) In a purchase transaction the amount of the loan shall be determined in accordance with Paragraph-6-2b above.

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- (2) In a refinancing transaction the amount of the loan shall be the lesser of:
- (a) An amount not to exceed 85 percent of the Secretary's estimate of value of the project.
 - (b) The maximum per unit limitation for new construction under Section 207 of the Act plus cost not attributable to dwelling space.
 - (c) An amount which entails a debt service not in excess of 85 percent of the net annual income as estimate by the Secretary.
 - (d) The cost to refinance the project as defined in Paragraph 6-2c(4) (b) above.

6-3. TERM OF MORTGAGE AND COMMENCEMENT OF AMORTIZATION.

- a. 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. Accordingly, the mortgage term shall be the eligible number of whole years between 10 and 35. Any fraction of a year shall be disregarded.
- b. Amortization shall commence on the first day of the second month following the date of the initial/final endorsement of the mortgage for insurance under the LAMP Plan.

6-4. IDENTITY OF INTEREST. In purchase transactions where there is a change in the ownership of existing property incident to the filing of the application for a commitment, a determination must be made as to whether any identity of interest exists between the seller and the purchaser. If there is any identity of interest, regardless of how slight, the application shall be processed as a refinancing transaction. (See Paragraph 6-2c for criteria.) The amount used as existing indebtedness shall be the allowable amount of the indebtedness on the property existing prior to the change in ownership.

6-5. DETERMINATION OF THE MAXIMUM INSURABLE MORTGAGE AMOUNT. The maximum insurable mortgage amount shall be established subject to the limitations in Paragraphs 6-2b, c, d, and e above. This shall be accomplished by the MCE completing
Criteria 1, 3, 4, 5, 7 (purchase

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* only), and 10 (refinancing only) of Form 2264-A. The instructions for the completion and addition of Criterion 7 and Criterion 10 to the Form 2264-A are found in reference (7) of the Foreword. In refinancing transactions where the project is located in an older, declining urban area, the debt service criterion will be computed as described in Paragraph 7-4 of this handbook.

6-6. RESERVE FOR REPLACEMENTS. The initial deposit to the Reserve Fund for Replacements shall be eligible for inclusion in determining the maximum insurable mortgage in a purchase transaction and in a refinancing transaction. If a Reserve Fund for Replacements has already been established for the project under consideration, the funds on deposit shall be used first to reduce the required deposit, with the excess, if any, applied toward the reduction of any discounts, miscellaneous fees, etc., that are included in the mortgage. In order to avoid possible duplication of costs, the following shall be required:

a. Purchase Transaction.

- (1) The purchase agreement must specify whether or not the acquisition price includes the purchase, as an asset of the project, of any Reserve Fund for Replacements or other escrows that may be on deposit with the mortgagee and must specify the dollar amount of such escrows that are being transferred with the sale.
- (2) The purchase agreement must specify any and all items which the seller will pay on behalf of the mortgagor, e.g., the operating deficit, discounts, the initial deposit to the Reserve Fund for Replacements, etc., and the dollar amount, if any, that will be contributed.
- (3) In order to ensure that the required initial deposit to the Reserve Fund for Replacements will be included in the mortgage (if the deposit will be funded by the purchaser), the MCE shall include the amount of the HUD required deposit on the appropriate line of Criterion 7 on Form 2264-A. If as a result of the disclosures required in (1) and (2) above, the MCE determines that a Reserve Fund for Replacements was transferred to the new mortgagor as an asset of the project, then the MCE shall apply the amount currently on deposit as a reduction when computing Criterion 7.

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b. Refinancing Transaction.

- (1) The mortgagor is required to submit a list of all escrows currently on deposit with the mortgagee. All such escrows must remain with the project.
- * (2) In computing Criterion 10, the MCE shall include the required initial deposit to the Reserve Fund for Replacements in the mortgage on the appropriate line.
- (3) If the analysis of the escrow statement reveals that the mortgagor currently has funds on deposit in a Reserve Fund for Replacements, the MCE will apply the amount currently on deposit as a reduction when computing Criterion 10 on FHA Form 2264-A.
- (4) The commitment shall carry the requirement that the balance in the existing Reserve Fund for Replacements account must be applied to the initial deposit to the Reserve Fund for Replacements; and that any excess shall be applied as a reduction to the costs of discounts, miscellaneous fees and charges, etc., which have been included in the determination of the maximum insurable mortgage.

6-7. EXHIBITS TO BE FORWARDED TO MORTGAGE CREDIT. The following required exhibits as specified in Paragraph 2-7 of this Handbook shall be forwarded to Mortgage Credit and shall become part of the credit control binder:

a. Conditional Stage.

- (1) Form 2013, Application for Project Mortgage Insurance.
- (2) The Rent Roll.
- (3) Balance sheets, operating statements, "Statements of Changes in Financial Position."

b. Firm Stage.

- (1) Form 2013, Application for Project Mortgage Insurance.
- (2) Form 3433, Request for Preliminary Determination of Eligibility As Nonprofit Sponsor or Mortgagor, if applicable. *

- (4) The statement reflecting the balance in all existing escrow accounts.
- (5) The statement reflecting identities of interest.
- (6) The evidence from the mortgagee regarding permanent mortgage financing.
- * (7) A copy of the legal documents creating the mortgagor entity. (A copy must be forwarded to the Area Counsel for review and comment.)
- (8) A copy of the Purchase Agreement.
- (9) The updated Rent Roll.
- (10) Balance sheets, operating statements, "Statements of Changes in Financial Position."
- (11) Form 2417 or equivalent.
- (12) The statement reflecting all debt service requirements.
- (13) The title search report.

6-8. PREAPPLICATION CONFERENCE. The MCE must participate in the preapplication conference to discuss the Mortgage Credit exhibits required to be submitted at the firm commitment stage and to answer any questions regarding the various aspects of mortgage credit processing.

6-9. FINANCIAL AND CREDIT ANALYSES. The fundamental credit consideration in the analysis of an existing multifamily project transaction involves the determination at firm commitment stage that the mortgagor has the financial capacity to provide the necessary equity to complete the loan transaction, liquidate the mortgage debt and successfully operate the project. This determination is based upon the analysis of current financial statements submitted by the mortgagor together with appropriate supporting schedules (which include an aging of accounts receivable). Commercial and individual credit reports shall be ordered at the time the firm application is received by the Mortgage Credit Staff. As in any Mortgage Credit analysis, decisions regarding credit and financial acceptability shall be made on a project by project basis.

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- * a. If the mortgagor entity has been formed and capital has been paid in prior to the issuance of a commitment, financial statements of the mortgagor entity shall be analyzed in accordance with sound analytical credit practices. The analysis shall

determine the adequacy of this capital to meet the financial requirements to which the mortgagor entity may be obligated.

- b. The MCE shall closely analyze the balance sheet entry for "accounts receivable." If the "accounts receivable" entry includes rents, the MCE shall request an aging of the receivables and a listing of the tenants from whom the rents are due and the units occupied by those tenants. This information shall be needed when the operating deficit is established. (See Paragraph 6-13 below).
- c. In those instances where the mortgagor entity has not been formed prior to the issuance of a firm commitment, it shall be necessary that the financial statements of the principals, submitted in accordance with reference (9) of the Foreword, be analyzed to determine the availability of funds for investment in the mortgagor entity. These funds may include operating capital readily available for investment purposes and/or other assets that may be readily hypothecated to produce investment capital.
- d. The accumulated credit data, together with the analysis made by the MCE of the financial statements, are reviewed to determine that the mortgagor is financially able to provide assets which together with the mortgage loan proceeds will be adequate to meet the requirements of the project, including cash deposits for the operating deficit.

6-10. SECONDARY FINANCING. For projects processed under Section 223(f), secondary financing shall be permitted as follows:

- a. Purchase Transaction. When a loan is made to refinance the purchase of an existing multifamily housing project, the mortgagor may not have any additional obligations in connection with the transaction which exceed the lesser of:
 - (1) Seven and one-half percent (7.5%) of the Secretary's estimate of value, or
 - (2) Seven and one-half percent (7.5%) of the cost of acquisition as defined in Paragraph 6-2b(4).

Such additional obligations may only be represented by a HUD approved "Promissory Note", Form 2223. *

(6-10)	Example 1.	Fair Market Value	\$2,000,000
		7-1/2% of Value	\$ 150,000
		Cost of Acquisition	\$2,200,000
		7-1/2% of Cost of Acquisition	\$ 165,000
		Maximum Amount Permitted to be	

Financed thru Promissory Notes \$ 150,000

Example 2. Fair Market Value \$2,000,000
7-1/2% of Value \$ 150,000
Cost of Acquisition \$1,900,000
7-1/2% of Cost of Acquisition \$ 142,000
Maximum Amount Permitted to be
Financed thru Promissory Notes \$ 142,000

b. Refinancing Transaction. When a loan is made to refinance an existing multifamily housing project, the mortgagor may not have any additional obligations in connection with the transaction which exceed the lesser of:

- (1) Seven and one-half percent (7.5%) of the Secretary's estimate of value; or
- (2) Fifty percent (50%) of the difference between the cost to refinance as defined in Paragraph 6-2c(4)(b) and the maximum mortgage amount as determined by the Secretary. (If this difference is \$99 or less, the mortgagor may not use promissory notes to satisfy the cash requirements.)

Such additional obligations may only be represented by a HUD approved "Promissory Note," Form 2223.

Example 1. Fair Market Value \$2,000,000
85% of Value \$1,700,000
Cost to Refinance \$1,900,000
Maximum Mortgage Amount \$1,700,000
Maximum Amount Permitted to be
Financed thru Promissory Notes \$ 100,000
Lesser of (a) \$2,000,000
x.075
\$ 150,000

or (b) \$1,900,000
-1,700,000
\$ 200,000
x .50
\$ 100,000

(6-10) Example 2. Fair Market Value \$2,000,000
85% of Value \$1,700,000
Cost to Refinance \$2,100,000
Maximum Mortgage Amount \$1,700,000
Maximum Amount Permitted to be
Financed thru Promissory Notes \$ 150,000
Lesser of (a) \$2,000,000
x.075
\$ 150,000

or (b) \$2,100,000
 -1,700,000
 \$ 400,000
 x .50
 \$ 200,000

Example 3. Fair Market Value \$2,000,000
 85% of Value \$1,700,000
 Cost to Refinance \$1,650,000
 Maximum Mortgage Amount \$1,650,000
 Maximum Amount Permitted to be
 Financed thru Promissory Notes \$ 0
 Lesser of: (a) \$2,000,000
 x.075
 \$ 150,000

or (b) \$1,650,000
 -1,650,000
 \$ 0

Example 4. Fair Market Value \$2,000,000
 85% of Value \$1,700,000
 70% of Value \$1,400,000
 Cost to Refinance \$1,300,000
 Maximum Mortgage Amount \$1,400,000
 Maximum Amount Permitted to be
 Financed thru Promissory Notes \$ 0
 Lesser of: (a) \$2,000,000
 x.075
 \$ 150,000

or (b) \$1,300,000
 -1,400,000
 (\$ 100,000)

c. In both purchase and refinancing transactions, if the cost of acquisition or cost to refinance decreases for any reason, the maximum allowable amount of promissory notes must be recomputed. For example, in a purchase transaction, the seller may lower the purchase price in order to reduce the buyer's front money requirements. Also, in a refinancing transaction, the financing plan may reveal that a portion of the indebtedness has been forgiven in order to reduce the mortgagor's front money requirements. In either case, the permissible amount of promissory notes must be recomputed.

* 6-11. FINANCING PLAN. After the cash requirements have been established, the MCE shall contact the mortgagee to advise that the mortgagor must submit a financing plan detailing how the cash requirements will be met. This plan must be submitted within ten working days after contact with the mortgagee.

- a. Promissory Notes. If a promissory note(s) will be utilized to retire any portion of the cash requirements, the financing plan must disclose to whom the note(s) will be issued and the amount(s) of each. Any other source(s) of capital must also be identified; the amount to be obtained from each source must be specified; and verifications from the source(s) involved must accompany the plan.
- b. Indebtedness Forgiven. Further, if any portion of the indebtedness will be forgiven, verifications from the appropriate lenders must accompany the plan.
- c. Action When the Conditional Commitment Stage Has Been Used. In refinancing or purchase transactions where a conditional commitment has been issued, the MCE shall review the financing plan to determine its acceptability. If review of the plan discloses that the financing arrangements are unsatisfactory as submitted or if the plan is not submitted within the required period, the MCE will reject the application for a firm commitment and forward the completed Form 2264-A and attachments to the Director of Housing Development.
- d. Action When the Conditional Commitment Stage Has Been Bypassed. In refinancing or purchase transactions where the conditional commitment stage has been bypassed and application is made directly for a firm commitment, the MCE shall review the financing plan to determine its acceptability. If review of

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the plan discloses that the financing arrangements are unsatisfactory as submitted or if the plan is not submitted within the required period, the MCE shall reject the application for a firm commitment. The MCE shall then advise the Director of Housing Development in writing of the reason(s) for the rejection and of the overall financial condition of the mortgagor. Provided it is otherwise warranted, a conditional commitment shall then be issued which shall:

- (1) Specify the reason for the Mortgage Credit rejection of the application for firm commitment,
- (2) Contain a statement of the results of the Mortgage Credit analyses of the financial statements and a listing of the estimated cash requirements, and
- (3) Required submission of an acceptable financing plan when the application for a firm commitment is resubmitted.

6-12. DISCOUNTS. For purposes of Section 223(f), discounts may be eligible for inclusion in the determination of the maximum insurable mortgage. The MCE shall review the documentation submitted by the mortgagee regarding permanent financing. Such documentation will state the amount of the discounts charged and to whom they will be paid. If the MCE determines that the stated discounts are reasonable and are in line with prevailing market conditions and Mortgage Credit data, they may be included in the determination of the maximum insurable mortgage subject to the following limitations:

- a. In a refinancing transaction, where there is an identity of interest between the present permanent mortgagee or the interim mortgagee and the new permanent lender, no additional financing charges other than the 2 percent financing fee and 1 1/2 percent placement fee shall be eligible for inclusion.
- b. In a purchase or refinancing transaction where an identity of interest exists between the mortgagee and the mortgagor, no additional financing charges other than the 2 percent financing fee and 1 1/2 percent placement fee shall be eligible for inclusion. *

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- * c. In a refinancing or purchase transaction, discounts shall be recognized only for those actual costs charged by the permanent lender which are determined to be eligible. Discounts charged for warehousing a mortgage for future delivery as well as those which may be charged by the interim lender are not eligible for inclusion.
 - d. In a refinancing or purchase transaction where an identity of interest exists between the mortgagees, and the GNMA Mortgage-Backed Securities Program will be used for permanent financing, discounts as determined reasonable by the MCE may be included. GNMA charges a \$500 fee for usage of this program. This fee may be included in the mortgage and may be designated as a permanent lender's placement fee. In no event, however, shall the 1 1/2 percent placement fee normally included in the mortgage for FNMA/GNMA be eligible for inclusion.
 - e. If the GNMA Mortgage-Backed Securities Program will be used for permanent financing, a sum equal to 1 3/4 percent of the mortgage amount must be placed in escrow for three years. This sum shall not be eligible for inclusion in the determination of the maximum insurable mortgage, but will be a cash requirement to the mortgagor, notwithstanding any identity of interest which may or may not exist

between any of the parties.

6-13. DETERMINING THE OPERATING DEFICIT. The amount of the operating deficit, if any, shall be determined at the firm commitment stage.

- a. If the conditional commitment stage was used, the MCE shall review the updated Rent Roll comparing it to the Rent Roll submitted at the conditional commitment stage. The review shall include a telephonic spot check of five percent (5%) of the occupied units to ascertain if the information contained in the updated Rent Roll is correct. The MCE shall identify those tenants contacted and the results of the conversations in the appropriate section of the Rent Roll. If there is inadequate space on the Rent Roll, the MCE shall record any remarks and reconcile any differences on a separate sheet and attach it to the Rent Roll. If there are a significant number of discrepancies or if the telephonic

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responses are unsatisfactory, the MCE must arrange for a visit to the project to complete the verification of the rent roll. If the occupancy has changed, the MCE shall notify the Director of Housing Development and Valuation staff so that, if necessary, adjustments may be made to the estimate of time needed for the project to reach sustaining occupancy.

- b. If application is made directly for a firm commitment, the MCE shall not review the Rent Roll for accuracy, since this task will have been performed by the Appraiser during the HUD Team's visit to the project.
- c. The period required for the project to reach sustaining occupancy shall be entered in the "Remarks" section of Form FHA-2264; and the amount determined as the operating deficit (using the Form FHA-2264 instructions found in reference (7) of the Foreword) shall be prorated accordingly. In no event may an operating deficit be established for more than eighteen months. If the appraiser indicates that it will take longer than eighteen months for the project to reach sustaining occupancy, the application must be rejected.
- d. If the project reaches sustaining occupancy prior to the expiration of the escrow period, the mortgagor, through the mortgagee, may petition HUD for permission to release the balance of the operating deficit escrow account. However, in no event may the escrow be reduced prior to the initial/final endorsement of the loan for insurance.

6-14. OPERATING DEFICIT ESCROW. If an escrow is required to cover an operating deficit at the time of endorsement, Form FHA-2476-A, "Escrow Agreement - Additional Contribution by Sponsors," must be furnished, showing the deposit of cash, an unconditional irrevocable letter of credit issued to the depository by a banking institution, or United States bearer bonds at market value. The acceptance of a letter of credit in lieu of cash or United States bearer bonds is within the discretion of the mortgagee and the burden is on the mortgagee to provide cash if demand on a letter of credit is not met. The conditions for release of the funds are contained in Form FHA-2476-A.

a. In the event of a claim under the contract of mortgage insurance, HUD shall not accept an assignment of a letter of credit from the mortgagee, but shall treat any undrawn balance thereunder as cash held by the mortgagee which will be deducted from the insurance claim.

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b. The enforceability of a letter of credit is the sole responsibility of the mortgagee and no opinion as to its enforceability is to be rendered by the closing attorney. However, the Field Office Director and the closing attorney have the responsibility to review and determine the sufficiency and acceptability of the escrow agreement.

6-15. COMMITMENTS. Commitments shall be issued on an Insurance Upon Completion Basis only. There shall be only one closing, combining both the initial and final endorsement of the insured mortgage transaction, and all mortgage proceeds shall be disbursed at that time. In the event that there are any required repairs which remain incomplete at the time of endorsement, an escrow account equal to twice the estimated cost of such repairs shall be established under the provisions of an Escrow Deposit Agreement, Form FHA-2456.

6-16. MORTGAGE INCREASES AND CHANGE ORDERS. It is possible that the field office may receive requests for mortgage increases for projects to be insured pursuant to Section 223(f).

a. Such requests may be processed provided all the following criteria are satisfied:

(1) The increase is a result of requirements imposed by the local municipality which were unknown when the required repair list was developed by HUD.

(2) The additional costs do not cause the cost of the repairs to exceed the limitations as set forth in

Paragraph 1-4 of this Handbook. (In the event that the cost of repairs will exceed the 15% or \$3,000 limitation as a result of the additional requirements, the commitment shall be null and void, and the mortgagor should be encouraged to apply for insurance under one of HUD's rehabilitation programs.)

- (3) The requested increase is accompanied by a change order, plus documentation from the municipality attesting that the work must be done in order that the property will comply with local laws and codes.

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- b. In such cases, once the additional repairs and the costs attributable thereto have been accepted and approved, the MCE shall process Form FHA-2264-A completing the applicable criteria and determine a new maximum insurable mortgage. If adjustments to the income flow become necessary the Form FHA-2264 and Form FHA-2264-A shall be forwarded to HM for review and comments.
- 6-17. COST CERTIFICATION. A modified form of cost certification shall be completed and submitted to the HUD field office for review 15 days prior to the initial/final endorsement of the loan for insurance for all projects processed pursuant to Section 223(f) except those refinancing transactions where 70% of value is the controlling criterion. (In such cases cost certification is not required.)
- a. Using Form FHA-2205-A (Exhibit VII), the mortgagor must certify to the total actual costs incurred in the acquisition or refinancing of the property. The certification must be dated and signed by an authorized agent of the mortgagor entity.
 - b. The MCE shall review the submission to establish the maximum insurable mortgage amount. Any disallowances shall be explained on a separate worksheet and attached to Form FHA-2205-A. The MCE shall complete Section II of Form FHA-2205-A.
 - c. The general contractor will only be required to submit a cost certification if a cost-plus form of contract is used.
 - d. If, in a purchase transaction, the amount of the acquisition cost determined allowable at cost certification exceeds the HUD estimate of value of the project determined during processing, instructions in paragraph 5-19 require that the rent formula be recomputed by the Valuation staff. In order that the

Valuation staff may accomplish this recomputation, the Mortgage Credit staff shall prepare a memorandum to the Chief, Valuation staff setting forth (1) the allowable acquisition cost as determined by cost certification and (2) the dollar amount of secondary financing represented by the approved promissory notes (Form FHA-2223).

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- 6-18. REQUIREMENTS PRIOR TO FINAL ENDORSEMENT. Prior to final endorsement, the mortgagee must provide the field office with all required closing exhibits including Form FHA-2455, Request for Endorsement of Credit Instrument Certificate of Mortgagee, Mortgagor and General Contractor, and a certified loan closing statement signed by the mortgagee and mortgagor detailing the amount of any promissory notes made by the mortgagor and any cash contribution made by the mortgagor. The statement must also itemize the disbursement of the mortgage proceeds and of the mortgagor's cash contribution, if any. The statement regarding the disbursements must be specific and list the amounts to be paid to satisfy the mortgagor's obligations for: existing or other indebtedness in a refinancing transaction; acquisition cost in a purchase transaction; repairs; discounts; financing fees; legal expenses; organizational expenses; title and recording costs etc., and any mortgagee required escrows for GNMA, taxes, or insurance.
- a. The MCE shall review the certificate of the mortgagee contained in Form FHA-2455 for the amounts reflected for the operating deficit and the financing charges. The MCE shall also review the amounts reflected in the mortgagee's certified statement regarding the disbursements, the promissory notes, etc. and shall compare the amounts reflected on Form FHA-2455 and the mortgagee's statement to those reflected on the cost certification. If the amounts are less than those shown on the cost certification, a recomputation of the mortgage amount shall be necessary in order to determine if a reduction to the maximum insurable mortgage amount shall be required.
 - b. Should such a reduction be necessary, a revised Part II of Form FHA-2205-A must be prepared by the MCE and delivered to the Director of Housing Development who shall advise the closing attorney, the mortgagee, and the mortgagor. If secondary financing is to be utilized to satisfy a portion of the cash requirements, a reduction in the permissible amount of promissory notes may also be required. A recomputation of the maximum amount of promissory notes permissible must be made using the format provided by Form FHA-2264 in reference (7) of the Foreword.

6-19. REQUIREMENTS AFTER FINAL ENDORSEMENT. Funds placed in escrow for incomplete repair items will be disbursed by the mortgagee upon approval by HUD. Upon the disbursement of all funds, the mortgagee will notify HUD by letter that all escrowed funds have been properly disbursed.

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