CHAPTER 9. FINAL CLOSING

SECTION 1. GENERAL.

9-1. INTRODUCTION. Upon expiration of 30 days after completion of construction to allow time for lien clearance, the Area Manager should initiate final closing of the Section 202 direct loan. However, if the Borrower desires to close at an earlier date, and if the title company issues a title policy which is free of all liens, then the Field Office should take the necessary steps to close before expiration of the 30-day waiting period.

9-2. ADVICE ON JUNIOR LIENS. The Area Manager shall not close the loan with outstanding junior liens without furnishing all facts and an Area Counsel's opinion to the Director, Office of Multifamily Housing Development, Headquarters, who will advise the Area Manager of the final administrative decision.

9-3. EXCEPTION TO TITLE. Any exception to title, not shown in the title evidence accepted at initial closing, which affects the use of marketability of the project should be examined carefully by the Field Office. If a clear determination cannot be made that the exception does not adversely affect the value of the property, the question should be submitted to the Director, Office of Multifamily Housing Development, Headquarters, for resolution.

9-4. COMPLETION FOR FINAL CLOSING DEFINED. Completion, for the purpose of final closing, means that:

a. The project has been completed in accordance with the contract documents, except for approved delayed completion items covered by an acceptable escrow agreement; and

b. The entire project has been accepted for occupancy by the local authorities having jurisdiction and by HUD.

9-5. PREPARATION FOR FINAL CLOSING. Upon the determination that a loan disbursement is, or will be, the last draw prior to disbursement of the holdback (or at the time of substantial completion, whichever is earlier) preparation for final closing should begin. At this point, it should be possible to make the determinations required by paragraphs 9-8, 9-10, 9-13 and 9-16. The Area Counsel shall be advised with respect to these determinations and of the time estimated to be necessary to complete the computations required by paragraphs 9-23 and 9-24. The MHR also shall advise the Borrower in writing with a copy to the Area Counsel. The Area Counsel shall
then advise the Borrower of the instruments and requirements for final closing. Pre-final closing activities shall also include participation by the Loan Management Branch to assure that the Borrower has complied with all management requirements.

9-6. DELINQUENCY IN INTEREST AND AMORTIZATION PAYMENTS. As part of the preliminary preparation for final closing, the Field Office shall communicate with the Regional Accounting Division to determine whether the Borrower is current in its construction interest and monthly amortization payments, if already commenced. Should there be any defaults, the Area Manager will contact the Borrower to bring current all delinquent accounts. Final closing shall not be permitted until all defaults have been rectified.

9-7. DATE FOR FINAL CLOSING. Upon completion of review of the certification of actual cost and upon preparation of Form 2580, Maximum Insurable Mortgage, the Area Manager will advise the Borrower and Area Counsel of his/her findings and establish a final closing date acceptable to all parties.

SECTION 2. PROPERTY INSURANCE REQUIREMENTS

9-8. CHANGES IN INSURANCE REQUIREMENTS. Immediately before execution of Form HUD-92403-EH, Requisition for Disbursement of Section 202 Loan Funds, for a final disbursement, the Area Manager shall ascertain whether any changes in drawings and specifications, or any appreciable change in the cost of construction of the project, have occurred during the course of construction which require a revision of Property Insurance Schedule, Form HUD-92329.

9-9. ACTION ON REVISED FORM. If it is not necessary to revise the previous Form HUD-92379, the Area Manager shall take no action with respect to property insurance. If a revision of Form HUD-92329 is necessary, the Area Manager, at the time of execution of Form HUD-92403-EH, shall forward revised copies of Form HUD-92329 to the Borrower with an appropriate letter advising the Borrower to substitute the revised copies (identifying such revised form by date) for the previous Property Insurance Schedule. Copies of the revised Forms HUD-92329 and related correspondence shall be filed in the Field Office Docket. Additionally, copies of the following shall be forwarded to the Insurance Advisory Branch, Office of Public Housing and Indian Programs, which has responsibility for monitoring the Section 202 property casualty insurance documents.

a. Latest Form HUD-92329,

b. Form FHA-2326, Project Cost Estimate, prepared subsequent to cost certification, and
c. Certified copies of all required permanent insurance policies and fidelity bond.

SECTION 3. INCOMPLETE ON-SITE FACILITIES.

9-10. CONDITIONS FOR APPROVAL. Ideally, all on-site construction should be 100 percent complete before approval of a final loan disbursement. There may, however, be circumstances where it is necessary or desirable to approve the final disbursement before 100 percent completion of on-site construction.

a. Approval of a final disbursement before full completion will be given only in cases in which minor items of on-site construction are incomplete and will be coupled with a requirement that funds be placed in escrow to assure completion of such minor items, as provided in the certificate of approval to disburse loan funds on Form HUD-92403-EH.

b. Approval of a final loan disbursement, moreover, will be given only in those cases in which:

(1) All on-site items in the entire project are completed, except those which qualify as delayed completion items, as set forth in underwriting architectural procedures;

(2) All off-site utilities such as sewer, water, electrical, and gas facilities are installed and connected, and the buildings are served by safe and adequate all-weather facilities (either permanent or temporary) for the ingress and egress of pedestrian and vehicular traffic, including fire apparatus, and all other construction requirements have been acceptably accomplished or acceptably assured;

(3) The Housing Director recommends that funds be placed in escrow for the completion of minor items because immediate completion is inadvisable or impossible, due to weather or other conditions beyond control; and

(4) The aggregate estimated cost of completing the above items does not exceed 2 percent of the loan amount.

9-11. ESCROW FOR COMPLETION. With respect to all incomplete items, the amount held in escrow for completion must be at least one and one-half (1-1/2) times the estimated cost of completion. The amount of any escrow shall be sufficient to assure an incentive to complete the work, taking into consideration a possible rise in cost. Such escrow will be held by HUD or its designee in accordance with the terms of the Escrow Deposit Agreement, Form FHA-2456, and the Area Manager will ascertain that the items to be completed are properly identified by attachment to Form
9-12. CONDITIONS FOR PAINTING ESCROW. In order to enhance rentability, and if acceptable to the Housing Director, an escrow may be established to cover the cost of final interior painting of apartments without regard to the usual 2 percent of the loan amount limitation on escrows previously mentioned. This is conditioned upon the builder being bound to complete all work covered by the approved plans and specifications within a fixed period of time (not to exceed one year from the date of final closing) and without any additional charge either to the Borrower or to the incoming tenants.

9-13. DISTINCTION BETWEEN FORMS OF ASSURANCE. When a request for approval of final disbursement is received in a case in which off-site facilities are incomplete a distinction must be made between those cases in which the assurance of installation and completion is in the form of a cash escrow, and those cases in which such assurance is in another form.

a. When the completion and installation of off-site facilities is assured by a cash escrow, and all off-site sewer, water, electrical and gas facilities are completely installed and connected, and other off-site facilities such as streets, walks, curbs, and gutters are incomplete but safe, and adequate facilities for ingress and egress are provided, the final loan disbursement may be approved. The Area Manager will require that the escrow agreement remain in force and will diligently pursue the completion of off-site facilities as assured by the escrow.

b. In those cases in which the assurance is in a form other than a cash escrow; the final disbursement of loan funds cannot be approved. Instead, the Area Manager

9-14. OFF-SITE UTILITIES. If off-site utilities are completely installed and connected, and ingress and egress is provided, the request for final disbursement may be treated as an ordinary application for a loan disbursement and may be approved in an amount which, when added to previous disbursements, will equal 90 percent of the total disbursements to which the Borrower will be entitled at 100 percent completion. In such cases:

a. Form HUD-92403-EH, will not be treated as approval of a final disbursement.
b. Following 100 percent completion of all off-site facilities, the Area Manager will require submission of a new Form HUD-92403-EH for approval of the final disbursement.

c. The Field Office staff will endeavor to obtain completion at the earliest possible time.

SECTION 4. NONREALTY ITEMS AND ALTERNATIVE SECURITY INSTRUMENTS

9-15. NONREALTY ITEMS. Prior to final closing, the Area Manager will forward to the Borrower and the Area Counsel a list of easily movable items which would be included in the nonrealty category. Among these are ranges, refrigerators, washers, dryers, water heaters, dishwashers, venetian blinds, removable air conditioning units, lobby and office furniture and similar items necessary for the operation of the project. All such items must be covered by the mortgage lien, whether or not paid for with loan funds, so long as such items are required in the operation of the project.

9-16. ALTERNATIVE SECURITY INSTRUMENTS.

a. The loan commitment (Form FHA-2432-EH) requires the Borrower at final closing obtain either:

(1) An attorney's opinion that the so-called nonrealty items are covered by the lien of the real estate mortgage or

b. The Area Counsel is responsible for obtaining either an acceptable opinion from the Borrower's attorney or the chattel mortgage or other security instrument.

c. Under the Uniform Commercial Code the security instrument or agreement is accompanied by a Financing Statement. In those jurisdictions where the Code is in effect, copies of both will be obtained if they are used.

9-17. CONTINUATION STATEMENT. The Financing Statement discussed above must be renewed periodically by the filing of a Continuation Statement under the Uniform Commercial Code and the enacting state laws. Procedures relating to Continuation Statements are set forth in the HUD-Held Servicing Handbook 4360.1, Chapter 7, Section 2. Upon receipt of an executed Continuation Statement from the Borrower, the Loan Management staff must forward a copy to the Regional Accounting Division.

SECTION 5. COST CERTIFICATION.
9-18. GENERAL. Cost certification is required by HUD regulations in all Section 202 projects. Only costs which have been paid in cash or will be paid in cash upon release of the balance of loan proceeds are eligible certifiable costs. Cost certification is completed in accordance with HUD Handbook 4470.2, Cost Certification Guide for Mortgagor and Contractors of HUD-Insured Multifamily Projects, except as modified herein.

9-19. JOINT PRE-COST CERTIFICATION CONFERENCE. The Cost and Mortgage Credit staffs shall hold a joint pre-cost certification conference with the Borrower, general contractor, and accountant when the project has attained a construction completion percentage of no more than 90 percent. At this conference, provisions of this chapter and of HUD Handbook 4470.2 shall be explained and the Borrower and contractor shall be asked to submit the required statements and certifications. The importance of a careful review by all parties, including the Borrower and accountant, prior to submitting the cost certification documents to HUD shall be stressed. Particular emphasis shall be placed on the necessity for completeness of the required documentation, dates and signatures and upon the timeliness of the submission.

9-20. REQUEST FOR SUBMISSION OF CERTIFICATION. The Area Manager will notify the Borrower, in writing, of the completion date for determination of actual costs. The Field Office will request submission of cost certification within a reasonable time and will include in the letter a statement that Properly documented cost certifications must be in the Field Office 30 days before final closing. One copy of the letter shall be sent to the Office of Multifamily Housing Development, Headquarters, one copy filed in the Field Office Docket, and one copy in the Area Counsel's file.

9-21. FORM OF COST CERTIFICATION. The documentation required from the Borrower will vary with the size of the mortgage and the type of construction contract.

a. If the construction contract is competitively bid, the Borrower must submit a Borrower's/Mortgagor's Certificate of Actual Cost, showing the actual cost to the Borrower of the construction contract, architectural, legal organization, offsite costs, and all other eligible expense items.

b. If the construction contract is not competitively bid, the Borrower must submit, in addition to the Certificate of Actual Cost identified in a above, a certification of the general contractor (and such subcontractor, material suppliers, and equipment lessors, as the Field Office determines appropriate), as to all actual costs paid for labor, materials, and subcontract work under the general contract.
c. The Certificate of Actual Cost required by paragraph a and b above must be verified by an independent public accountant acceptable to the Field Office.

d. If the project mortgage is $500,000 or less, regardless of whether the construction contract is competitively bid, the Borrower must submit a simplified form of cost certification.

9-22. OPERATING STATEMENT. If there has been occupancy during the period of construction, an audited operating statement is required. The period covered is from first occupancy of the project to the cut-off date for the inclusion of interest, taxes, and property insurance premiums. (See Handbook 4470.2 for definition of cut-off date and items to be included in the statement.) If this operating statement produces excess operating income, such net income up to $25,000 shall be transferred at final closing to a residual receipts account for future project needs. (Note: The current Section 202 Regulatory Agreement does not provide for a residual receipts account, but future revision will incorporate this account.) Any net income in excess of $25,000 shall be transferred to the reserve fund for replacements.

9-23. SUPPLEMENTAL INCOME STATEMENT. When more than ninety days will intervene between the cut-off date for cost certification and the first scheduled principal payment under the mortgage, a supplemental statement of income and expense is required. The supplemental statement must cover the period from the cut-off date to a date three months prior to the start of amortization. Any net income will be treated in the same manner as discussed in paragraph 9-22, above.

SECTION 6. CONTRACT RENTS

9-24. DETERMINATION OF CONTRACT RENTS.

a. Upon completion of the review and acceptance of the certificates of actual cost, the Field Office will determine whether a reduction in contract rents is appropriate.

(1) If the certified cost is equal to or in excess of the cost approved at initial loan closing, no change in contract rents will be made.

(2) If the certified cost is less than the cost approved at initial loan closing, appropriate reductions in contract rents and any corresponding reduction in the Section 8 contract and budget authority will be calculated.

b. If a reduction in contract rents is required:
(1) The MHR shall prepare a letter to the Borrower enclosing an original and two copies of an amended contract rent schedule (Exhibit 1 to the Contract).

(2) If contract and budget authority is also to be reduced:

(a) The Legal Division will prepare for enclosure with the letter any additional amendment documents necessary to effect the reduction and

(b) A revised HAP contract will be prepared and forwarded along with the letter RAD for confirmation of the reduction.

(c) Upon execution by the Borrower, all copies of the amended contract rent schedule and any other required Contract amendment documents will be returned to the Field Office for execution by the Housing Director.

(d) If contract rents are reduced, pursuant to paragraph b above, after HAP Contract execution, any overpayment after the effective date of the Contract will be recovered from the Borrower.

SECTION 7. SECTION 202 LOAN

9-25. DETERMINATION OF MAXIMUM LOAN AMOUNT.

a. Before Final Closing. On completion of the review of certificates of actual cost and acceptance thereof, the Area Manager shall notify the Borrower whether or not a reduction in the original amount of the mortgage is necessary by the issuance of Form FHA-2580, Maximum Insurable Mortgage.

(1) Follow-up for Supplemental Certification. If at final closing a supplemental certification is required for items "to be paid in cash within 45 days," an appropriate follow-up for obtaining the certification must be established.

(2) Review and Action on Supplemental Certification. Supplemental statements, certified by an accountant in the
same manner as the original submission, are required for any estimated costs allowed in the original cost certification. They are also required for any items "to be paid in cash within 45 days." These statements are reviewed by the Field Office staff under the same conditions as followed in review of the Form FHA-2330, Mortgagor's Certificate of Actual Cost.

(a) When this supplemental certification is received, the Field Office staff shall determine whether or not an adjustment in the mortgage amount is required. This is ascertained by substituting actual costs for the amounts estimated in the original certification of costs (before final closing) and computing a new maximum loan.

(b) Any prepayment on the mortgage required as a result of this supplemental cost certification is mandatory. Instructions set forth in the cost certification procedures with respect to mandatory prepayments will apply to this prepayment.

9-26. EXCESS LOAN PROCEEDS. There is a possibility that actual disbursements for a project may be less than the approved loan. In such circumstances a reduction of the loan amount shall be required.

9-27. APPLICATION FOR FINAL LOAN DISBURSEMENT. When final disbursement is in order, the Borrower will execute the completed Form HUD-92403-EH and the form will be submitted by the Borrower in triplicate. The form shall be accompanied by: (1) a completed Contractor's Requisition, Form FHA-2448; (2) Contractor's Prevailing Wage Certificate, Form FHA-2403-A; (3) a final survey; (4) Request for Final Endorsement of Credit Instrument, Form FHA-2023; and (5) Escrow Deposit Agreement, Form FHA-2456, if necessary.

3/83 Page 9-10

4571.1 REV-2

CHAPTER 9

(9-27) a. The survey accompanying this request must show the exact location of all buildings, water, sewer, gas and electric mains, and all easements for such existing utilities. It must be prepared by a registered professional land surveyor who must certify that the project is installed and erected entirely on the land covered by the mortgage and within the building restriction lines, if any, on said land, and does not overhang or encroach upon any easement or right-of-way of others.

b. On receipt, all copies of the Form and attachments will be routed to the technical staff, processed, and submitted to the Area Manager. Since this will be the final disbursement of loan proceeds, the Area Manager will determine whether:
(1) Any items of on-site construction are incomplete;

(2) Any off-site facilities are incomplete;

(3) Any revisions are required in connection with hazard insurance; and

(4) The necessary chattel mortgage or certificate of Borrower's attorney has been submitted (as required by paragraphs 9-15 and 9-16 of this Chapter) and will be guided accordingly.

c. If no on-site construction items are incomplete, "None" shall be entered in the "Certificate of Approval" block on Form HUD-92403-EH. If on-site construction items are incomplete and an escrow deposit (in accordance with paragraph 9-11) is in order, attach to Form HUD-92403-EH an itemized list of incomplete items; and type the amount of the escrow deposit required to complete the listed items in the "Certificate of Approval" block.

d. The Form FHA-2023 completed and executed by the Borrower and general contractor must be submitted in triplicate. (The front portion of the Form shall be modified appropriately and completed by the Borrower.)

(1) The Form FHA-2023 will be checked against each previously approved Form HUD-92403-EH to determine that the amount of each disbursement is correctly stated and that the total shown on the Form FHA-2023 equals the total of all disbursements. If any error is found, the form will be returned to the Borrower with an explanation of the correction required. When reviewing this form, the Area Manager should examine the title evidence submitted prior to final closing to confirm the certification by the Borrower as to items of outstanding indebtedness.

(2) The Borrower and general contractor shall be advised of their obligations concerning certifications and the penalty provided by law for misstatements. Form FHA 2023 requires in every case a full disclosure by both the Borrower and the general contractor of all outstanding unpaid obligations. In addition, in cases where during the construction there is strong evidence of slow payment or nonpayment by Borrower or the general contractor, it is within the discretion of the Area Manager to require that sufficient funds from the loan disbursement be placed in escrow for
disbursement to satisfy all unpaid obligations disclosed on Form FHA-2023 and attachments. Such funds are to be released from escrow only upon being furnished with simultaneous acknowledgement of payment by the general contractor and/or appropriate subcontractor or materialman. However, in all cases the Field Office shall proceed as follows:

(a) Borrowers shall be advised that all unpaid obligations contracted in connection with the acquisition of land, purchase of property, construction of the project, or the loan transaction shall without exception be reported on Form FHA-2023 as required by the Certificate of the Mortgagor. Likewise, general contractors shall be advised that all unpaid obligations under the construction contract shall be reported on Form FHA-2023 as required by the Certificate of the General Contractor.

(b) The unpaid obligations of the Borrower listed under (b) and (c) of paragraph 2 of the Certificate of the Mortgagor on Form FHA-2023 shall not exceed the amount of the final loan disbursement. In the event that a Form is received showing an excess, it shall be returned to the Borrower advising that the differences must be liquidated by cash payment or through the issuance of a promissory note. A corrected Form FHA-2023 must then be submitted. If a Promissory note is used, it must be on the proper HUD-FHA prescribed note form and no change in substance shall be permitted.

(c) In any case where the general contractor certified unpaid obligations general contractor exceed the amount certified by the Borrower as due the general contractor, the Area Manager shall urge the prompt payment of such excess obligation.

e. The approved Form HUD-92403 shall be transmitted to the Regional Accounting Division for necessary processing to obtain the Treasury check for the final disbursement.

9-28. FINAL CLOSING. When the application for final disbursement has been processed and approved, the final closing conference should be scheduled. The credit instrument will be finally closed in an amount equal to the full amount of all disbursements to the Borrower, as shown by the applicable Form FHA-2023, regardless of
whether the final closing occurs before or after the commencement of amortization.

9-29. REQUESTING AMORTIZATION SCHEDULE. Immediately after final closing, Form FHA-2409, Amortization Schedule Request, will be prepared. When the Form has been completed and reviewed and the certification signed, it will be forwarded to the Regional Accounting Division (RAD) together with a completed copy of Form FHA-2023, Request for Final Endorsement of Credit Instrument. RAD shall produce the amortization schedule and make distribution of the schedule as provided in Handbook 1970.39, Accounting and Reporting Requirements for Section 202 Direct Loan Program for Housing for the Elderly or Handicapped.

9-30. ASSURANCE OF PERFORMANCE UNDER GUARANTEE. The Construction Contract, Form FHA-2442A-EH, contains a guarantee against any defects due to faulty materials or workmanship which appear within a period of one year following completion. The date of completion is defined as the date the HUD Representative signs the 100% completion Inspection Report. The Area Manager will be careful to avoid any action that might invalidate or limit the contractor's guarantee.

9-31. CASH ASSURANCE. If a Completion Assurance Agreement, Form FHA-2450-EH, was used at initial closing, the Area Manager may, at final closing, release the escrow funds except for an amount equal to 2-1/2 percent of the total amount of the construction contract. The retained percentage shall be held in the escrow account during the one-year guarantee period as specified in Form FHA-2450-EH. The escrow here provided for is separate and apart from any escrow that may have been provided to assure completion of any incomplete construction items.

9-32. OTHER ASSURANCE. If either Form FHA-2452-EH, Performance Payment Bond (Dual Obligee), or Forms FHA-2452, Performance Bond, and FHA-2452A, Payment Bond, were used, no action is required at final closing.

9-33. CHRONOLOGY. At final closing, the Area Manager will be responsible for preparation and furnishing of two copies of Form FHA-260, Chronology of Mortgage Transactions, to the Area Counsel, who will attach it to the Closing Memorandum, Form FHA-290, and promptly send these Forms to the Office of the General Counsel for review and distribution to the Director, Office of Multifamily Housing Development, Headquarters. In addition, a copy of the chronology will be filed in the Field Office Docket.

SECTION 9. DISPOSITION OF CLOSING DOCUMENTS
9-34. HEADQUARTERS LOAN MANAGEMENT DOCKET. Subsequent to final closing, a loan management docket consisting of copies of the following documents shall be prepared for transmittal to Headquarters:

1. Regulatory Agreement (Form FHA-2466-EH)

2. Mortgage (or deed of trust) (Form FHA-2099-EH)

3. HAP Contract

4. Closing Memorandum (Form FHA-290)

5. Amortization Schedule.

The completed file shall be sent to the Office of Multifamily Financing and Preservation, Department of Housing and Urban Development, Washington, D.C. 20410.

9-35. LOAN TRANSCRIPT DOCUMENTS. The Loan Transcript consists of documents as listed on Appendix 30. Immediately after final closing, the Area Manager shall send to the Regional Accounting Division (RAD) by certified mail any documents on the list which have not been previously provided. Any modification of the applicable documents will also be included in the transmittal. The transmittal memorandum to RAD shall account for all items on the Loan Transcript (Appendix 27) with specific notations as to which documents have been submitted earlier.

9-36. PREPARATION OF FIELD OFFICE DOCKET. After Preparation of the Loan Transcript, all remaining original and duplicate material, including executed or conformed copies of the material listed in Appendix 30, will be filed in the Field Office Docket. The contents of the Field Office Docket are to remain in chronological order. None of the documents contained in the docket may be destroyed until the loan is paid off and the mortgage is terminated. Subsequent to final closing, the Field Office Docket will be transferred to the Loan Management Branch for custody during the project operation phase.

SECTION 10. MANAGEMENT REVIEW.

9-37. ON-SITE MANAGEMENT REVIEW WITHIN 6-MONTH PERIOD SUBSEQUENT TO ALL UNITS BEING AVAILABLE FOR OCCUPANCY.

a. An appropriate management team shall make an on-site management review within the 6-month period subsequent to the date when all units are available for occupancy. The team shall make a complete review of project operations including:
(1) Physical condition.

(2) Maintenance Program.

(3) Evaluation of implementation of Management Plan. (If social services are provided in the Management Plan, the Neighborhood and Consumer Affairs Representative shall be included in the review team to evaluate their implementation.)

(4) Spot check of tenant certifications.

(5) Adequacy of bookkeeping system.

(6) Review for developing problems.

b. This team review will be in addition to the regular Latent Defects Inspection. A written report covering the results of the inspection, including the necessary remedial actions being taken, will be submitted to the Housing Director with a copy to the Area Manager.