

SMALL BUILDING RISK SHARING INITIATIVE

I. PROGRAM DETAILS

A. How the Initiative Works

Qualified QPEs are authorized to underwrite and process loans. HUD will provide full mortgage insurance on affordable multifamily housing projects processed by such QPEs under this Initiative. By entering into a Risk Sharing Agreement (RSA) with HUD, the QPE contracts to reimburse HUD for 50 percent of any loss from defaults that occur while HUD insurance is in force.

B. Commitment Authority Availability

Commitment Authority availability is provided by the Congress on an annual basis for all multifamily and health care insured loans, including those in the Risk Sharing Program. In rare circumstances it may become necessary for HUD to notify Risk Sharing partners that HUD is approaching its congressionally determined subsidy volume cap and provide instructions for reservation and obligation of subsequent Commitment Authority.

C. Execution of the Risk Sharing Agreement (RSA)

Execution by the QPE of an RSA is prerequisite to participation in this Initiative, because it governs the rights and obligations of HUD and the QPE. The letter from HUD to the QPE approving its participation in the Risk Sharing Program will transmit the RSA for execution by an authorized representative of the QPE (i.e., one who is so designated in the application). The original signed RSA and an electronic copy must be returned to HUD Headquarters, Office of Multifamily Housing Production. Headquarters will transmit a copy of the executed RSA to the applicable designated office of the QPE.

D. Program Requirements under the Initiative

1. Affordable Housing Requirements

All projects, under this Initiative must qualify as “affordable housing” under the Risk Sharing Program; the definition is generally consistent with the requirements of the Section 42 LIHTC Program. Specifically, projects financed with Risk Sharing loans must have 20 percent or more of the units rent-restricted and initially occupied by families whose income is 50 percent or less of the area median income, with adjustments for household size, or 40 percent or more of the units rent-restricted and initially occupied by families whose income is 60 percent or less of the area median income, with adjustments for household size. The Initiative affordability requirements also include the following elements:

- a. New tenants must be eligibility certified only when they sign an initial lease. Whenever such a tenant moves out, a new tenant who will occupy the same or a comparable unit to be considered part of the set-aside units must be eligibility certified at move in as well. Annual re-certifications are not required.
- b. Rents for the set-aside units must not exceed 30 percent of 50 percent or 60 percent of area median income, adjusted for family size, depending on the set-aside selected, as required by the Risk Sharing Program.
- c. The building owner does not need to permanently designate specific units for this affordable designation. However, the units included must be distributed proportionately through the building’s various unit types (for example, if 40 percent of the units are to be set aside for tenants earning no more than 60 percent of median income, then the units counted for purposes of compliance must include 40 percent of all 1-bedroom units, 40 percent of all 2-bedroom units, etc. and may not, for example, include only the lowest rent apartments.)

Accordingly when a tenant moves out of one of the rent-restricted units, the replacement unit need not be the same one, but should be of the same type/size in order to maintain the equal distribution of set-aside units across unit types.

d. These affordability requirements will be satisfied and enforced primarily through an affordability restriction placed on title and lasting for the life of the Risk Sharing Loan.

2. Eligible Projects

a. Project Site. Projects must consist of 5 or more rental dwelling units (including cooperative dwelling units) on one site. The site may consist of two or more noncontiguous parcels of land situated so as to comprise a readily marketable real estate entity within an area small enough to allow convenient and efficient management. These units may be detached, semi-detached, row houses, or multifamily structures.

b. Loan Size. Loan amounts may not exceed \$3 million or, \$5 million in “High Cost Areas” annually designated by HUD.

c. Lender’s Loan Limits. QPEs will be limited to a maximum of twenty (20) closed loans or \$50 million in closed loans, whichever occurs first, during their first year of participation in the Initiative as measured from the date of execution of their Risk Sharing Agreements. After the first year, HUD will evaluate program risk and review the QPE’s compliance with program requirements. If satisfactory, this limit may be adjusted or eliminated.

d. Substantial Rehabilitation. Substantial Rehabilitation is work to the existing facilities of a project that results in material improvement of the project's economic life, livability, marketability, and profitability as further defined in the MAP Guide in “Architectural and Construction Analysis”.

e. Existing Projects. Financing of existing properties without substantial rehabilitation is permitted so long as all of the capital needs in the Capital Needs Assessment (CNA) and the reserve requirements for the life of the loan are addressed. If the property has a loan to be refinanced in the Risk Sharing transaction and such refinancing will result in the preservation of affordable housing, refinancing is permissible so long as all of the following conditions are met: 1) project occupancy is not less than 93 percent, including consideration of rent in arrears, based on the average occupancy in the project over the most recent 12 months, and 2) the mortgage does not exceed an amount supportable by a) the lower of the unit rents being collected under the rental assistance agreement, or b) the unit rents being collected at other unassisted projects in the market area similar in amenities and location the project for which insurance is being requested.

f. Single Room Occupancy (SRO). SRO projects are eligible for insurance in the Initiative. Units in SRO projects must be subject to 30-day or longer leases, but rent payments may be made on a weekly basis in SRO projects.

3. Ineligible Projects

a. Transient Housing or Hotels. (“Rental for transient or hotel purposes.”) Under this Initiative, rental for transient or hotel purposes means: 1) Rental for any period less than 30 days, or 2) Any rental, if the occupants of the housing accommodations are provided customary hotel services such as room service for food and beverages, maid service, furnishing and laundering of linens, and valet service.

b. Projects in Military Impact Areas. If the HUD local Office determines that a project is located in a military impact area, the project shall not be insured under this program.

- c. Retirement Service Centers. Projects designed for the elderly with extensive services and luxury accommodations and that provide for central kitchens and dining rooms with food service or mandatory services are not permitted in the Risk-Sharing Program.
 - d. Nursing Homes or Intermediate Care Facilities. Nursing homes and intermediate care facilities licensed and regulated by State or local government and providing nursing and medical care are prohibited.
 - e. Board and Care/Assisted Living Facilities. Board and Care/Assisted Living Facilities that provide continuous protective oversight and assistance with the activities of daily living for frail elderly or other persons needing such assistance may not be insured. These facilities typically provide room and board as well as oversight and assistance and contain a central kitchen and dining area, although meals may be catered off site.
4. Local Land Use Requirements. Projects insured under this Initiative must meet applicable zoning and other State/local government requirements.
 5. Prohibition on GNMA Securitization. Issuance of Ginnie Mae mortgage-backed securities is currently prohibited for projects insured under the Risk Sharing Program. This restriction may be lifted if proposed legislation is adopted.
 6. Appraisal Standards. Certified General Appraisers licensed in the State in which the property is located must complete all appraisal functions. All appraisal functions must also be completed in accordance with the Uniform Standards of Professional Appraisal Practices.
 7. Mortgage Insurance Premium. The mortgage insurance premium in effect at that time as established by the Commissioner and published in the Federal Register.
 8. Environmental Review. All projects insured under the 542(b) Risk Sharing Program must comply with the environmental requirements of 24 CFR Part 50. Based on materials collected

and provided by the QPE, HUD will conduct the environmental reviews in accordance with the MAP Guide. QPEs must assume all responsibilities of the lender under the MAP Guide in “Environmental Review and Requirements”, which include making various submissions related to contamination and the environmental laws and authorities listed at 25 CFR 50.4. The QPE, the owner and its contractors must not undertake any activities that would have an adverse environmental impact, limit the choice of reasonable alternatives, or prejudice the ultimate decision on the proposal until HUD has issued a Firm Approval Letter for the project. The Firm Approval Letter will include any special conditions, procedures and requirements resulting from the Environmental Review. Finally, the QPE must advise HUD of any proposed change in the scope of the project or any change in environmental conditions and shall ask HUD to conduct a supplemental environmental review for such change.

9. Labor Standards. Davis Bacon wage determinations are not applicable to the 542(b) Risk Sharing Program.

10. Byrd Amendment (Lobbying). The Byrd Amendment requires disclosure by mortgagors of lobbying activities for programs involving loan guarantees by the Federal government. Form LLL must be submitted with the closing docket required in paragraph 6-2 of Form LLL so that HUD can compile the material under the annual report required by the Byrd amendment.

11. Reinsurance. A QPE may obtain reinsurance for the portion of the risk of loss assumed by the QPE subject to the following requirements: a) Neither HUD's nor the QPE's position shall be subordinated to the rights of the reinsurer; b) The reinsurance may not be used to reduce any reserve or fund balance requirements that are required to be maintained under this Initiative; and c) Such reinsurance does not incur an obligation to the Federal Government.

12. Nondiscrimination and Equal Opportunity in Housing and Employment The mortgagor must

certify to the QPE that, so long as the mortgage is insured under the Risk Sharing Program, it will:

a) Not use tenant selection procedures that discriminate against families with children, except in the case of a project that constitutes housing for older persons as defined in Section 807(b)(2) of the Fair Housing Act (42 U.S.C. 3607(b)(2)); b) Not discriminate against any family because of the sex of the head of household and; c) Comply with the Fair Housing Act, as implemented by 24 CFR part 100; Titles II and III of the Americans with Disabilities Act of 1990, as implemented by 28 CFR part 35; Section 3 of the Housing and Urban Development Act of 1968 (12 U.S.C. 1701u), as implemented by 24 CFR part 135; the Equal Credit Opportunity Act, as implemented by 12 CFR part 202; Executive Order 11063, as amended, and implemented by 24 CFR part 107; Executive Order 11246, as implemented by 41 CFR part 60; other applicable Federal laws and regulations issued pursuant to these authorities; and applicable State and local fair housing and equal opportunity laws. In addition, a mortgagor that receives Federal financial assistance must also certify to the QPE that, so long as the mortgage is insured under this part, it will comply with Title VI of the Civil Rights Act of 1964, as implemented by 24 CFR part 1; the Age Discrimination Act of 1975, as implemented by 24 CFR part 146; and Section 504 of the Rehabilitation Act of 1973, as implemented by 24 CFR part 8.

Such certification does not preclude HUD, the QPE, or a HUD-delegated agent from monitoring or reviewing the project's compliance with nondiscrimination or equal opportunity requirements including, but not limited to, preparing or updating an Affirmative Fair Housing Marketing Plan or maintaining records of housing applicant or resident race, national origin, or disability status.

II. FIRM APPROVAL LETTER PROCESSING

A. General

The QPE will submit as part of its request for issuance of a Firm Approval Letter, a request for

HUD to begin the HUD-retained reviews and other findings to the Multifamily Regional Center or Satellite Office with jurisdiction for the location of the project, to include:

1. The QPE's HUD Mortgagee Number
2. Environmental. A Phase I Environmental Site Assessment, Environmental Report, and other documentation required by the FHA MAP Guide in “Environmental Review and Requirements”. (A Firm Approval Letter may not be conditional on subsequent environmental review), and
3. Other HUD Reviews Sufficient information about the project for the HUD Office to conduct the previous participation, environmental, intergovernmental and other HUD-retained reviews. Successful completion of the HUD retained reviews results in issuance by HUD of a Firm Approval Letter.

B. Processing

1. Initial Processing
 - a. QPE’s Mortgagee Number. The FHA-approved mortgagee number is the identifier for the QPE in the Federal Housing Administration Subsidiary Ledger (FHASL) system, and in the Development Application Processing (DAP) System. The Multifamily Regional Center or Satellite Office should use the mortgagee identification number on all correspondence.
 - b. Project Number. The Multifamily Regional Center or Satellite Office is responsible for entering basic project data in the DAP system to create a new application and FHA project number when the request for Firm Approval Letter is received. The QPE will provide detailed information related to the project’s location, number of units, and other identifying materials necessary. The project number is based on the location and program identifier (Section of Act Code) and contains the following identifying information: 1) The 3-digit HUD office prefix for HUD’s Regional Center or Satellite Office which identifies the

specific geographic location of the project, 2) project number series in a range to be determined, and 3) Section of Act (SOA) Code identifier that will consist of one or more new, three digit codes to be assigned to the Initiative.

2. Environmental Review. All projects insured under the 542(b) Risk Sharing Program must comply with the environmental requirements of 24 CFR Part 50. QPEs must make various submissions with the request for issuance of a Firm Approval Letter related to contamination and the environmental laws and authorities listed at 25 CFR 50.4, in accordance with the Lender requirements of the MAP Guide. HUD will conduct the environmental reviews in accordance with the MAP Guide. The QPE must not undertake any activities that would have an adverse environmental impact, limit the choice of reasonable alternatives, or prejudice the ultimate decision on the proposal until HUD has issued a Firm Approval Letter for the project.

3. Intergovernmental Review. The QPE is responsible for sending the form SF-424 to the appropriate State Single Point of Contact (SPOC) if the State has selected the mortgage insurance programs for review under the intergovernmental State Review Procedure (SRP) and the project proposes insured advances. Substantial rehabilitation projects with insured advances are covered only if there is 1) a change in land use, 2) an increase in project density, or 3) a change from rental housing to cooperative housing. The Catalog of Federal Domestic Programs number for the Risk Sharing Program is 14.189. NOTE: Many States do not review insured projects under these procedures. If the State has not elected the mortgage insurance programs for review, the QPE should submit a statement to that effect. If comments are received from the SPOC, the following applies:

- a. When the SRP results in favorable comments or a recommendation for approval, the Regional Center or Satellite Office may issue the Firm Approval Letter if all other HUD-

retained review requirements are met. The Regional Center or Satellite Office must apply the "non-accommodation" procedures if, for other reasons, the Regional Center or Satellite Office will not issue the Firm Approval Letter (e.g., adverse environmental review).

b. When the SRP results in negative comments or a recommendation for disapproval, if the Regional Center or Satellite Office agrees with the SRP, it will tell the QPE what changes are necessary before the Firm Approval Letter may be issued, or that no Firm Approval Letter may be issued. If the Regional Center or Satellite Office disagrees, paragraph c. below applies and the Regional Center or Satellite Office will advise the QPE that the Firm Approval will be held until the 15-day "Non-accommodation" period ends.

c. "Non-accommodation" of SRP comments. The Regional Center or Satellite Office must notify the State and provide a 15-day period before 1) approval and issuance of a Firm Approval Letter, or 2) if the Regional Center or Satellite Office does not accept the SRP recommendation or 3) the QPE notifies HUD that it elects not to approve the project. HUD will notify the QPE at the same time, stating when the 15-day period ends and that a Firm Approval Letter may be issued or the project rejected after the 15-day period ends. NOTE: All notifications between the QPE and the Multifamily Regional Center or Satellite Office must be in writing.

4. Issuance of Firm Approval Letter. Upon positive completion of the HUD-retained reviews, the Multifamily Regional Center or Satellite Office will issue a Firm Approval Letter and send a copy to the QPE. The Firm Approval Letter will, among other things, identify the risk levels to be assumed by the QPE as 50 percent, and by HUD as 50 percent. The Firm Approval Letter also states that, absent fraud or material misrepresentation by the QPE, provided the QPE is in good standing at the time of the requested endorsement, and subject to adjustment of the mortgage amount, if required, HUD will endorse the project mortgage upon receipt of the complete closing

docket. Finally, the Firm Approval Letter may contain conditions for approval. The QPE and mortgagor must evidence their acceptance of the Firm Approval Letter and any conditions by signing and returning the Firm Approval Letter to the Multifamily Regional Center or Satellite Office.

The Firm Approval Letter will expire after one year if the project has not reached initial endorsement for insured advances projects, final endorsement for existing projects, or start of substantial rehabilitation for insurance upon completion projects. The Regional Center or Satellite Office may extend a Firm Approval Letter upon written request of the QPE with supporting documentation.

The Multifamily Regional Center or Satellite Office will prepare and transmit with the Firm Approval Letter, an addendum to the RSA reflecting the insurance risk share to be borne by the QPE and HUD, in the amount of 50 percent each.

In cases where the subsidy layering review is not delegated to the Housing Credit Agency and a HUD review is required, the Firm Approval Letter will require the QPE to submit the required documentation for that review before the QPE approves the loan under its own procedures if that documentation was not submitted with the request for HUD-retained reviews.

5. Rejection of Project. The Multifamily Regional Center or Satellite Office must notify the QPE in writing if the project is not approvable due to location in a military impact area, or for an adverse environmental condition that cannot be mitigated, or other adverse reasons that cause the project to be unfeasible.

III. PROGRAM PROCESSING

A. QPE Processing, Underwriting, and Substantial Rehabilitation

The QPE may use its own underwriting standards and loan terms and conditions, as disclosed

and submitted with its application to underwrite and approve loans without further underwriting review by HUD, so long as those terms are consistent with this exhibit and subsequent guidance as may be updated by HUD.

1. QPE Responsibilities. The QPE is responsible for the performance of all functions except the HUD-retained functions specified in this notice. After acceptance of an application for a loan to be insured under this Initiative, the QPE must, among other things:

- a. Determine that a market for the project exists, taking into consideration any comments from the Regional Center or Satellite Office relative to the potential adverse impact the project will have on proposed or existing Federally insured and assisted projects in the area;
- b. Establish the maximum insurable mortgage and review plans and specifications for compliance with QPE standards;
- c. Determine the acceptability of the proposed mortgagor and management agent, if any;
- d. Ensure the project is in compliance with all applicable nondiscrimination and equal opportunity laws (see program requirement under Section I.D.12);
- e. Make any other determinations necessary to ensure acceptability of the proposed project;
- f. Carry out all responsibilities of the Lender in connection with HUD's environmental review in accordance with the MAP Guide; and
- g. Ensure that any required subsidy layering review is completed by the applicable Housing Agency or HUD prior to loan approval.

2. Substantial Rehabilitation Period. The QPE is responsible for inspections during substantial rehabilitation, processing and approving advances of mortgage proceeds during substantial rehabilitation, review and approval of cost certification, and closing of the loan.

3. Inspections during Substantial Rehabilitation. The QPE must inspect projects at such times

during substantial rehabilitation as the QPE determines. The inspections must be conducted to ensure compliance with the contract documents.

4. Federal Labor Standards. Prevailing Wage Standards are not applicable to the 542(b) Risk Sharing Program.
5. Lead-Based Paint. Risk Sharing projects must comply with the lead-based paint requirements in 24 CFR Part 35, specifically subparts A, B, G, and R (Lead Disclosure Rule and Lead Safe Housing Rule), as applicable, as well as 40 CFR Part 745, Lead Renovation, Repair, and Painting Program. QPEs are responsible for monitoring and for ensuring that lead based paint requirements are followed.
6. Insurance of Advances. Periodic advances are permitted in the Risk Sharing Program. In periodic advances cases, progress payments approved by the QPE and both an Initial and Final endorsement on the mortgage are required.
 - a. Advances may only be used for projects involving substantial rehabilitation.
 - b. In approving advances, the QPE must ensure that the loan is kept in balance, and advances are approved only if warranted by substantial rehabilitation progress evidenced through QPE inspection, as well as in accord with plans, specifications, work write-ups and other contract documents. QPEs must also make certain that other mortgageable items are supported with proper bills and/or receipts before funds can be approved and advanced for insurance.
7. Insurance upon Completion. In insurance upon completion cases, only the permanent loan is insured and a single endorsement is required after satisfactory completion of substantial rehabilitation or repairs. Existing projects without the need for substantial rehabilitation are only insured upon completion.

- a. Substantial rehabilitation. The QPE approval of an insurance upon completion project must prescribe a designated period during which the mortgagor must start substantial rehabilitation. If substantial rehabilitation is started as required, the approval will be valid for the period estimated by the QPE for substantial rehabilitation and loan closing, including any extension approved by the QPE.
- b. Existing projects without substantial rehabilitation and existing projects with or without repairs are insured upon initial closing. Capital needs identified in the CNA must be addressed through immediate repairs and/or reserves for the life of the loan. QPEs may permit noncritical repairs to be completed after endorsement upon establishment of escrows acceptable to the QPE. Noncritical repairs are those repairs that do not 1) endanger the safety and well-being of tenants, visitors and passersby or, 2) adversely affect ingress and egress, or 3) prevent the project from reaching sustaining occupancy.
- c. Cost Certification is required to ensure that the final amount of insurance is supported by certified costs. If there is an identity of interest with the mortgagor and general contractor, the mortgagor must execute a certificate of actual costs, in a form acceptable to the QPE, when all physical improvements are completed to the satisfaction of the QPE. The cost certification provided by the mortgagor must be audited by an independent public accountant in accordance with requirements established by HUD. Except for the first trial cases (described at Section IV.10) HUD will not review cost certifications prior to Final Endorsement. Subsequently cost certification documents will be looked at as part of HUD's periodic, programmatic monitoring of the QPE's risk sharing activities.
- d. Other Requirements. The mortgagor must furnish an assurance of completion in accordance with any requirements of the QPE as to form and amount, and a latent defects

escrow or other form of assurance as required by the QPE to ensure that latent defects can be remedied within the time period required by the QPE.

e. Recordkeeping. The mortgagor and the substantial rehabilitation contractor, if there is an identity of interest with the mortgagor, must keep and maintain records of all costs of any substantial rehabilitation or other cost items not representing work under the general contract and to make available such records for review by the QPE or HUD, if requested.

11. Project Information. QPEs are responsible for providing information about Risk Sharing projects to HUD for statistical, programmatic, and monitoring purposes. The project information is submitted with the closing docket at initial closing for insurance of advances cases, and/or final closing for insurance upon completion cases. When a substantial rehabilitation project will be insured upon completion, (i.e. no initial endorsement), project information must be submitted to the Multifamily Regional Center or Satellite Office when substantial rehabilitation begins. The cover letter should specify the substantial rehabilitation start date.

IV. CLOSING AND LOAN ENDORSEMENT

A. QPE Closing and HUD Endorsement of Loan

Before disbursement of loan advances in periodic advances cases, and in all cases after completion of repairs or substantial rehabilitation (or completion of processing for existing projects requiring no repairs), the QPE must hold a closing and submit a closing docket with required documentation to the Multifamily Regional Center or Satellite Office with jurisdiction for the project's location. The submission will include, among other things, the mortgage note which the Regional Center or Satellite Office Director will endorse for insurance. Prior to closing, the QPE must ensure that the following property and mortgage requirements have been met:

1. Property Requirements – Real Estate. The mortgage must be on real estate held:

- a. In fee simple;
 - b. Under a renewable lease of not less than 99 years; or
 - c. Under a lease executed by a governmental agency, or other lessor approved by the QPE, that has a term at least 10 years beyond the end of the mortgage term.
 - d. Marketable title to the mortgaged property must be vested in the mortgagor on the date the mortgage is filed for record.
 - e. The QPE must receive a title insurance policy (or other acceptable title evidence in the jurisdiction if title policies are not typical) that ensures that marketable title is vested in the mortgagor, that a survey acceptable to the QPE has been performed, and that no existing impediments to title concern, or exist on, the property.
2. Mortgage Provisions – and as referenced in Exhibit 1
- a. The mortgage and note must be executed on a form approved by the QPE for use in the jurisdiction in which the property is located. The note must provide that the mortgage is insured under Section 542(b) of the Housing and Community Development Act of 1992. The note must also specify the risk of loss assumed by the QPE and by HUD, at 50 percent each.
 - b. The mortgage must be executed by a mortgagor determined eligible by the QPE.
 - c. The mortgage must be a single first lien on property that has first priority for payment and that conforms to property standards prescribed by the QPE.
 - d. The mortgage must require that the mortgagor is a single asset, sole purpose mortgagor.
 - e. The mortgage may be fully amortizing with a term of not more than forty (40) years, or it may require a balloon payment of the outstanding principal no sooner than the end of year fifteen calculated on a term of no more than thirty (30) years. Commencement of

amortization must begin the month following HUD's endorsement of the loan in cases of insurance upon completion. Alternatively, in the case of insured advances, amortization must begin following HUD's final endorsement. Amortization may not commence prior to HUD loan endorsement.

f. Use Restrictions. The mortgage must contain a covenant prohibiting the use of the property for any purpose other than the purpose intended on the day the mortgage was executed.

g. Hazard Insurance. The mortgage must contain:

i. A covenant acceptable to the QPE that binds the mortgagor to keep the property insured by one or more standard policies for fire or other hazards which are stipulated by the QPE;

ii. A standard mortgagee clause making loss payable to the QPE must be included in the mortgage;

iii. The QPE is responsible for ensuring that insurance is maintained in force and in the amount required by this paragraph and by the mortgage;

iv. The QPE must ensure that the insurance coverage is in an amount which will comply with the coinsurance clause applicable to the location and character of the property, but not less than 80 percent of the actual cash value of the insurable improvements and equipment.

If the mortgagor does not obtain the required insurance, the QPE must do so and assess the mortgagor for such costs; and

v. These insurance requirements apply as long as the QPE retains an interest in the project and final claim settlement has not been completed or the contract of insurance has not been otherwise terminated.

vi. If the property is located in a Special Flood Hazard Area identified by the Federal

Emergency Management Agency and in which the sale of flood insurance has been made available under the National Flood Insurance Act of 1968 (NFIA), the QPE must ensure that the property is covered by flood insurance during the term of the mortgage in an amount equal to or greater than the least of the following: (1) the development or project cost less estimated land cost; (2) the maximum limit of coverage made available for the type of property under the NFIA; or (3) the outstanding principal balance of the mortgage.

h. **Regulatory Agreement.** The mortgage must contain a provision incorporating the Regulatory Agreement by reference. The Regulatory Agreement will contain a provision that, in the event of a claim, for a period of three years after the claim is filed with HUD, no residents have been evicted or displaced for other than good cause and the rents have not been raised above the LIHTC maximum rents.

3. Mortgage Lien and Other Obligations

a. **Liens:** At the initial and final closing of the loan, the mortgagor and the QPE must certify, and the QPE must determine, that the property covered by the mortgage is free from all liens other than the insured mortgage, except that the property may be subject to an inferior lien(s) as approved by the QPE, as long as the insured mortgage has first priority for payment.

b. **Contractual Obligations:** At the final closing of the loan, the mortgagor and the QPE must certify, and the QPE must determine, that all contractual obligations in connection with the mortgage transaction, including the purchase of the property and the improvements to the property, are paid. An exception is made for obligations that are approved by the QPE and determined by the QPE to be of a lesser priority for payment than the obligation of the insured mortgage.

4. Execution of Regulatory Agreement. The QPE and the mortgagor must execute and record a Regulatory Agreement in a form acceptable to HUD, a standard form of which will be developed by the QPE. The Regulatory Agreement must include an addendum requiring the mortgagor to comply with the requirements of the Risk Sharing Program for as long as the Commissioner insures the mortgage.

5. Submission of Closing Docket. The QPE must submit the closing docket, representations and certifications, to the Regional Center or Satellite Office transmitted by letter signed by an authorized official identified in the RSA. An original and one electronic copy must be submitted. The closing docket, each page numbered in the upper right corner with the HUD project number, must contain specific project information, and be accompanied by a check for the first year's Mortgage Insurance Premium.

a. Project Information. Project information concerning the mortgage amount, location, number and type of units, income and expenses, rents, rents as a percentage of area median income, project occupancy percentage, value/replacement cost, interest rate, type of financing, tax credit use (if applicable), and similar statistical information will be provided.

b. Initial Closing for Insured Advances. If an initial closing docket is required, it should be submitted by the QPE and must include the information and certifications requested in this Notice. The Regional Center or Satellite Office will review the initial closing docket in a manner similar to its review of the final closing docket.

c. Final Closing. After substantial rehabilitation completion of the project or completion of critical repairs (noncritical repairs may be made after final endorsement with establishment of appropriate escrows acceptable to the QPE) and execution of a certificate of actual cost (for both insurance of advances and insurance upon completion), the QPE will submit a

closing docket to the Multifamily Regional Center or Satellite Office for final endorsement.

The final closing docket must include the information and certifications required by this notice along with the QPE's updated project information if submitted for initial endorsement.

6. Local HUD Office Review of Closing Dockets. The Regional Center or Satellite Office has primary responsibility for review of closing dockets and ensuring that projects are endorsed for insurance. The Regional Center or Satellite Office has 5 working days to complete this process except for the sample of projects that the Office chooses for pre-endorsement monitoring, which has a 10-day deadline. However, every effort should be made to endorse projects as quickly as possible.
7. Certifications. Multifamily Housing staff will review all closing dockets for completeness, including the QPE's certifications that:
 - a. Written approval was obtained for all HUD-retained reviews; and
 - b. All nondiscrimination, equal opportunity, and equal employment opportunity requirements were followed;
 - c. The QPE reviewed and approved the mortgagor's Affirmative Fair Housing Marketing, processing, underwriting (including a determination that a market exists for the project), cost certification (at final closing only) and closing were all performed according to the QPE's standards and requirements;
 - d. For insurance of advances cases, advances were made proportionate to substantial rehabilitation progress;
 - e. The property is free of all liens other than the first mortgage except for inferior liens approved by the QPE; and
 - f. All contractual obligations are paid.

8. Other Information. The Regional Center or Satellite Office will review each closing docket for among other things, the presence of the QPE's project information, amortization schedule, a copy of the RSA with any prior amendments or addendums; certified copies of the mortgage (deed of trust), mortgage (deed of trust) note with the risk of loss to be assumed by the QPE and HUD specified on the face sheet; a copy of the QPE-approved cost certification; a copy of the Regulatory Agreement between the QPE and the mortgagor; and a hazard insurance policy with a clause making the loss payable to the QPE; (for final endorsement of insured advances), a copy of the QPE-approved schedule of insured advances equal to the Risk Sharing mortgage documenting the date and amount of each of disbursement during the substantial rehabilitation period. The Regional Center or Satellite Office will also determine that certifications and other documents committing the QPE were signed by QPE officials identified in the RSA.

9. Local HUD Office Monitoring Functions. The Regional Center or Satellite Office will perform pre-endorsement monitoring by reviewing a limited sample of the first three insured advances cases and cost certifications. The Regional Center or Satellite Office has a total of 10 working days to review the submission and endorse the mortgage for insurance for these sample cases. In the case of these initial submissions HUD has the authority to make an appropriate adjustment to the amount of mortgage insurance up to and including final endorsement. However, it is anticipated that adjustments would be made only in very rare cases (as they are rare for HUD-processed projects).

a. Insurance of Advances. Check to see whether advances were consistent with substantial rehabilitation progress, whether the loan remained in balance by comparing actual disbursements against a project completion schedule, and whether disbursements were supported by bills and/or receipts.

b. Cost Certification. Review the QPE's cost certification to ensure that the amount to be insured is supported by costs actually incurred and approved by the QPE.

10. HUD Endorsement. After review of the closing docket and other materials, the Multifamily Regional Center or Satellite Office must do the following:

a. Endorsement: Unless the loan is one of the first three initial cases submitted for HUD review before endorsement, the Regional Center or Satellite Office Director will endorse the credit instrument within 5 workdays after accepting the closing docket. The original endorsed credit instrument must be returned by certified mail, return receipt requested.

b. Mortgage Insurance Premium (MIP): The Regional Center or Satellite Office must issue an Official Receipt for the initial year's MIP from the QPE (mortgagee). The MIP for the Risk Sharing Program is different than HUD's other mortgage insurance programs.

c. Closing Memorandum. The Regional Center or Satellite Office staff is responsible for preparing the HUD-290 in DAP based on project data consistent with the closing docket. The Regional Center or Satellite Office Director, Operations Officer, or a person officially delegated to act for the Director signs the HUD-290, and includes the original with the original closing docket to be transmitted to Headquarters, and includes a copy with the conformed closing docket for the monitoring phase.

d. Contents of HUD-290 Closing Submissions. Within 5 workdays of endorsement, the Regional Center or Satellite Office Director must submit copies of the following documents to the HUD Headquarters Office of Multifamily Insurance Operations:

- i. Closing Memorandum Form HUD-290 signed by Director or designee;
- ii. Official Receipt Form HUD-27038 for the first mortgage insurance premium;

- iii. Schedule of Collections form HUD-3416 documenting the deposit of the first mortgage insurance premium;
- iv. Mortgage note or deed of trust including endorsement panel signed by officials of the QPE and HUD;
- v. Amortization schedule consistent with the terms described on the mortgage note or deed of trust;
- vi. Copy of the RSA with any prior amendments, and addendum to the RSA for the subject project; and
- vii. For final endorsement of insured advances only, a copy of the QPE-approved schedule of insured advances.

12. Transmittal of Washington Closing Docket. The Risk Sharing original closing docket is processed in the same manner as the Washington Docket is for projects insured under the National Housing Act except that the contents of the docket, including amortization schedule, must comply with the requirements of the Section 542(b) Risk Sharing Program. The closing docket must be delivered within 30 workdays of endorsement to Headquarters, Office of Housing, Chief, Records Management Branch (HOAMP), B-264, including:

- a. The cover memorandum and original HUD-290; and
- b. The closing docket prepared by QPE, with each page numbered.

13. Recordation. At the time of Initial Endorsement, in the case of insurance of advances, or at the time of Final Endorsement in the case of insurance upon completion, the QPE shall make certain that the mortgage, the Regulatory Agreement, and the Uniform Commercial Code financing statements are properly recorded, and filed in all required locations.

V. PROGRAM MONITORING

Periodic program monitoring will be performed at two levels: 1) The Multifamily Regional Center or Satellite Office with jurisdiction for the QPE, and 2) HUD Headquarters. HUD will conduct compliance monitoring in accordance with the QPE's own approved procedures for origination, underwriting, processing, servicing, management and disposition procedures, as well as compliance with HUD regulations and guidelines. Annual certifications will be required to verify that the necessary staffing, procedures, and measures of financial capacity addressed in the QPE's application for participation in the Initiative remain in effect. Other HUD offices may monitor QPEs and projects in accordance with their delegated authority including compliance with nondiscrimination, equal opportunity, labor, and environmental protection requirements. Monitoring will be performed on a remote and on-site basis primarily consisting of post-endorsement compliance reviews. The Regional Center or Satellite Office with jurisdiction for the QPE will have primary responsibility to conduct periodic on-site monitoring to determine overall compliance with program requirements.

HUD Headquarters' primary responsibility will be overall program evaluation and the review of documentation pertaining to continued compliance of the QPE with program eligibility requirements, including monitoring of the dedicated account, where applicable, and other financial requirements. As appropriate, HUD Headquarters, including the Multifamily Asset and Counterparty Oversight Division (MACOD) in the Office of Asset Management and Portfolio Oversight, and the Multifamily Claims Branch in the Multifamily Financial Operations Division in the Office of Financial Services may also be involved in conducting reviews of specific QPEs to determine compliance with applicable requirements.

QPEs must submit annual audited financial statements to HUD Headquarters (Office of Multifamily Production) and the Designated Office. In addition, the HFA must submit to Headquarters:

1. The semi-annual report on its portfolio insured under Section 542(b). This report must include the original mortgage amount and outstanding principal balance for all projects underwritten, the status of all projects (current, in default, workout, foreclosure, etc.) and, if applicable, the date(s) bankruptcy was filed and the date(s) the QPE requested dismissal;
2. An annual certification signed by an authorized signatory of the QPE that there has been no basic change in organization, business activities, financial status or other information submitted with its application for approval (or if changes, the nature of those changes) and that the QPE complied with all eligibility requirements during the past year. The certification must list the names of the QPE's underwriter(s), construction loan administrator(s), and authorized signatory(s) to bind the QPE on Risk Sharing applications, and include the following language: **WARNING: "HUD will prosecute false claims and statements. Convictions may result in criminal and/or civil penalties. (18 U.S.C. 1001, 1010, 1012; 31U.S.C. 3729, 3802)."**
3. Any change(s) to its standards and procedures, loan terms and conditions before implementation of such change(s), providing copies of any such change within 5 business days after it has been approved by the QPE. HUD Headquarters must review proposed changes and provide its written approval to the QPE before the QPE can implement the change(s).
4. Other information necessary to ensure compliance with program requirements and performance of the QPE in meeting program objectives.

VI. PROJECT MANAGEMENT AND SERVICING

A. General

The QPE is responsible for providing loan servicing and project management in conformance with the RSA and the terms of the required Regulatory Agreement.

1. QPE Responsibilities. As it relates to project management and loan servicing, the responsibility of the QPE shall include, but not be limited to:

a. Execution and Enforcement of Regulatory Agreement. Execution and enforcement of a Regulatory Agreement between the mortgagor and the QPE that is recorded upon the closing of the Risk Sharing Loan and which:

- i. Includes a description of the property;
- ii. Is binding upon the mortgagor and any of its successors and assigns and upon the QPE and any of its successors for the duration of the insured mortgage. The QPE may not assign the Regulatory Agreement;
- iii. Requires the project owner to make all payments due under the mortgage and, where necessary, establish escrows and reserves for future capital needs;
- iv. Requires the project owner to maintain the project as affordable housing;
- v. Requires the project owner to maintain the project in good physical and financial condition;
- vi. Requires the project owner to maintain complete project books and financial records, and provide the QPE with annual audited financial statements after the end of each fiscal year;
- vii. Requires the project owner to comply with the Fair Housing Act, Titles II and III of the Americans with Disabilities Act of 1990; Section 3 of the Housing and Urban

Development Act of 1968, the Equal Credit Opportunity Act, Executive Orders 11063 as amended by Executive Order 12259, Executive Order 12246, other applicable federal laws and regulations issued pursuant to these authorities, and applicable state and local fair housing and equal opportunity laws; and, if the mortgagor receives federal financial assistance, requires the project owner to comply with Title VI of the Civil Rights Act of 1964, the Age Discrimination Act of 1975, and Section 504 of the Rehabilitation Act of 1973, and HUD's regulations issued pursuant to these laws;

vii. Requires the project owner to operate as a single asset mortgagor entity; and

viii. Requires the project owner to make project books and financial records available for HUD's Inspector General and FHA Commissioner and his/her duly authorized agents, and/or Government Accountability Office (GAO) for review with appropriate notification.

- b. Physical Inspections. Performing annual physical inspections of the project and providing a copy of the inspection reports upon request to the local Regional Center or Satellite Office. If the project receives a less than satisfactory rating and/or if the project is not in safe and sanitary condition, the QPE must provide a summary to HUD of the actions required within two weeks of the inspection. This summary must address both critical (health and safety related) and non-critical repairs, if any, along with target dates to correct unresolved findings.
- c. Analyzing project annual audited financial statements and providing HUD with a summary of any unresolved or negative findings, including a summary of corrective actions planned, with target dates. Providing HUD with an annual audited financial statement of the QPE in accordance with the requirements of 24 C.F.R. § 85.26 Non-Federal audit and OMB Circular A-133 "Audits of States, Local Governments, and Non-Profit Organizations".

2. Record Retention: Records pertaining to the mortgage loan origination and servicing of the loan must be maintained for as long as the mortgage insurance remains in force. Records pertaining to a mortgage default and claim must be retained from the date of default through final settlement of the claim and for a period of no less than 3 years after final settlement.

VII. MORTGAGE INSURANCE PREMIUMS AND FINANCIAL SYSTEMS

QPEs are responsible for processing Risk Sharing project applications and approving them for HUD mortgage insurance. The Regional Center or Satellite Office records project information in the DAP system and provides HUD Headquarters with data needed to establish the insured case in the FHASL System. The Multifamily Insurance Operations Branch (MFIOB) is responsible for tracking the portfolio of HUD insured projects and managing the collection of MIP. The MFIOB will bill QPEs for all premiums and applicable late fees and interest charges due subsequent to the MIP payment made at Initial Endorsement.

A. Establishing the Insurance in Force Record

1. Projects with Insured Advances. Projects endorsed with insured advances provide for HUD mortgage insurance coverage of funds disbursed during the substantial rehabilitation period.

a. Initial Endorsement. The Initial Endorsement of the mortgage note is performed by the Regional Center or Satellite Office and normally occurs prior to the start of substantial rehabilitation. Projects become part of the HUD- insured portfolio at this time.

QPE Responsibilities prior to Initial Endorsement include:

i. Collecting the Initial MIP: Prior to submitting projects to the Regional Center or Satellite Office for Initial Endorsement, the QPE will collect an MIP payment equal to the prescribed percentage of the insured amount. The QPE will instruct the mortgagor to make the MIP check payable to the U.S. Department of Housing and Urban Development;

- ii. Preparing the Closing Docket: The QPE will prepare a closing docket in accordance with instructions contained in this document. The closing docket will include the mortgage note, amortization schedule, and risk sharing agreement; and
- iii. Submitting the Endorsement Request to the Regional Center or Satellite Office: The QPE will mail the MIP along with the Closing Docket to the Regional Center or Satellite Office for endorsement of the mortgage note. These must be mailed within 15 days of closing.

Multifamily Regional Center or Satellite Office Initial Endorsement Responsibilities:

- i. Preparing the Official Receipt. The Regional Center or Satellite Office will deposit the MIP on the day received and prepare and distribute the Official Receipt, form HUD-27038 documenting the MIP payment and form HUD-3416 “Schedule of Multifamily Project Collections” documenting the deposit of the MIP payment;
- ii. Updating the DAP System. The Regional Center or Satellite Office will update the project data in the DAP system within 2 days of Initial Endorsement and prepare the form HUD-290 “Multifamily Closing Memorandum” to create the FHASL insurance in force file;
- iii. Reporting to the (MFIOB). Within 5 days of receipt of the Closing Docket from the QPE, the Regional Center or Satellite Office must forward documents required to establish the insurance record to the MFIOB. One copy each of the form HUD-290 “Multifamily Closing Memorandum”, amortization schedule, mortgage note, copy of the Risk-Sharing Agreement, form HUD-27038 “Official Receipt” and form HUD-3416 “Schedule of Multifamily Project Collections”; and copies of these documents will also be incorporated in the official Docket that the Regional Center or Satellite Office must submit to Headquarters.

The Regional Center or Satellite Office will submit the Official Receipt for the initial premium payment to the Office of Finance and Accounting (OFA).

iv. MFIOB Action. The MFIOB will process information received from the Regional Center or Satellite Office to establish the project in the FHASL System. The creation of a newly insured project in FHASL also requires certain information from the official receipt issued by the Regional Center or Satellite Office for receipt of the initial insurance premium. The FHASL record will be used to generate the annual MIP billings.

b. Final Endorsement. Projects with insured advances will be finally endorsed by the Regional Center or Satellite Office after completion of substantial rehabilitation. The terms of the mortgage note may be modified at this time as a result of substantial rehabilitation and cost certification.

QPE Responsibilities Prior to Final Endorsement:

- i. Preparing the Closing Docket. The QPE will prepare closing docket and submit project information in accordance with instructions contained in this notice. The docket will include the mortgage note, amortization schedule, RSA and any modifications to the original note, copy of the QPE-approved schedule of insured advances equal to the risk-sharing mortgage; and
- ii. Submitting the Endorsement Request to the Local HUD Office. The QPE will mail the Closing Docket to the Regional Center or Satellite Office for Final Endorsement of the note.

Multifamily Regional Center/Satellite Office Final Endorsement Responsibilities:

- i. Preparing the Closing Memorandum. The Regional Center or Satellite Office will update the DAP System and prepare the form HUD-290 within 2 days of endorsement. The form HUD-290 will reflect any changes to the mortgage terms that existed at the time of the

Initial Endorsement; and

ii. Reporting to MFIOB. Within 5 days of receipt of the Closing Docket from the QPE, the Regional Center or Satellite Office must forward one copy each of the Final Endorsement HUD-290, mortgage note, amortization schedule, schedule of insured advances equal to the final mortgage, RSA and modification agreement, if applicable

iii. MFIOB Actions. The MFIOB will process closing docket information received from the Regional Center or Satellite Office to process the final endorsement in FHASL.

2. Projects Insured Upon Completion. Projects endorsed with insurance upon completion are processed for insurance after completion of substantial rehabilitation, or purchase, or refinance with or without repairs for existing projects. Initial and Final endorsement of these cases occurs simultaneously.

a. Initial/Final Endorsement: Insured upon completion projects become HUD-insured at the initial/final endorsement.

QPE Responsibilities Prior to Initial/Final Endorsement:

i. Collecting the Initial MIP. Prior to submitting projects to the Regional Center or Satellite Office for Initial/Final endorsement, the QPE will collect the MIP payment. The QPE will instruct the mortgagor to make the MIP check payable to the U.S. Department of Housing and Urban Development;

ii. Preparing the Closing Docket. The QPE will prepare a Closing Docket in accordance with instructions contained in this notice. The docket will include the mortgage note, amortization schedule and RSA; and

iii. Submitting the Endorsement Request to the Regional Center or Satellite Office. Within 15 days of closing, the QPE will submit the MIP along with the Closing Docket to the

Regional Center or Satellite Office for endorsement of the mortgage note.

Multifamily Regional Center or Satellite Office Initial/Final Endorsement Responsibilities:

- i. Preparing the Official Receipt. The Regional Center or Satellite Office will deposit the MIP on the day received and prepare and distribute the Official Receipt and Schedule of Collections documenting the MIP payment in accordance with Handbook 4110.1, REV-1;
 - ii. Preparing the Closing Memorandum. The Regional Center or Satellite Office will update project data in the DAP System within 2 days of the Initial or Final Endorsement and prepare the form HUD-290;
 - iii. Reporting to MFIOB. Within 5 days of receipt of the Closing Docket from the QPE, the Regional Center or Satellite Office must forward documents required to establish the insurance record to the MFIOB;
 - a. Copies of Documents – Submitting one copy each of the form HUD-290, mortgage note, amortization schedule, the RSA, Official Receipt, and Schedule of Collections to MFIOB; and
 - b. Official Docket. Copies of these documents will also be incorporated in the official Docket that the Regional Center or Satellite Office must submit to Headquarters. The Regional Center or Satellite Office will submit the Official Receipt for the initial premium payment to the Office of Finance and Accounting (OFA) in accordance with instructions contained in Handbook 4110.1 Rev.
 - c. Processing Closing Docket Information. The MFIOB will process the closing docket information received from the Multifamily Regional Center or Satellite Office to establish the project in the FHASL System.
3. Annual Premium Billing and Record Change. Official records on HUD-insured multifamily

projects are maintained by the MFIOB in the FHASL System at HUD Headquarters. This organization also is responsible for billing and collecting annual mortgage insurance premiums. MIP is billed and collected in advance and under certain circumstances, in connection with termination of FHA mortgage insurance or prepayments, refunds of unearned premiums will be made to the QPE for the mortgagor's account. All modifications to the mortgage that take place after final endorsement, as well as mortgage servicer changes, will be recorded in the FHASL system.

- a. Annual Premiums: QPEs will be billed for all annual premiums due after the initial premium. All premium payments will be made through pay.gov in accordance with Mortgagee Letter 2012-16.
- b. Interim Premiums Pre-Amortization: Premiums calculated on the total insured amount will be due on the first day of the month of each anniversary of the initial endorsement that occurs prior to the date of first payment to principal. These interim premiums are only relevant for projects with insured advances where the first payment to principal date is more than 12 months after initial endorsement. The due date for interim premiums will be the first day of the month in which the anniversary of the initial endorsement occurs.
- c. Annual Premiums Post-Amortization: The annual MIP payments, beginning with the first payment to principal, will be calculated in accordance with the amortization schedule prepared by the QPE and supplied to HUD and the MIP Percentage taken from the Closing Memorandum prepared by the Regional Center or Satellite Office. The first regular annual premium will be due on the first day of the month in which the first payment to principal occurs. This first billing (as well as subsequent annual premiums) will be calculated by multiplying the QPE's annual MIP by the average outstanding principal balance during the

upcoming 12 months following first payment. This payment will reflect an adjustment to deduct any portion of the last interim premium paid that covers a period after first payment. Thereafter, until maturity or termination in this notice, MIP payments will be due on the first day of the month of each anniversary of the first payment to principal. The billings will be mailed to the servicing mortgagee of record approximately 45 days before the due date.

d. **Billing Statement and Reconciliation.** A sample billing statement is available in HUD Handbook 4590.1, Appendix 16. This form is to be returned along with the payment.

4. **Method of Payment.** Annual mortgage insurance premium payments must be made through pay.gov.

5. **Late Fees and Interest Changes.** All payments must be received no later than 15 days after the due date. Payments received after this will incur additional charges.

a. **Late Fees:** All premiums received by HUD more than 15 days after the due date will be assessed a 4 percent late charge.

b. **Daily Interest Charges:** Premiums that remain unpaid more than 30 days after the due date will accrue daily interest from the due date until paid at the rate prescribed by the Treasury Fiscal Requirements Manual. HUD will bill for interest and late fees each month until the charges are paid.

6. **Post Final Endorsement Modifications**

a. The QPE will provide the Regional Center or Satellite Office with a copy of the modification agreement along with a copy of the revised amortization schedule;

b. The Regional Center or Satellite Office will update the DAP System within 2 days of receipt of notification of the modification agreement;

c. The Regional Center or Satellite Office will forward copies of the modification agreement

and amortization schedule, and revised form HUD-290 to MFIOB;

d. The MFIOB will update FHASL to reflect the modified mortgage terms. Future premium billings will be calculated on the new terms; and

e. The QPE will be responsible for notifying HUD of any change in the project servicing mortgagee. Up-to-date mortgagee information is needed in order for HUD to properly direct premium billings and other project related correspondence. Mortgage changes will be accomplished by completing and forwarding form HUD- 92080 , “Mortgage Record Change” to:

U.S. Department of Housing and Urban Development

Multifamily Insurance Operations Branch

PO Box 44124

Washington, DC 20026-4124

7. Termination of Insurance: The QPE must remit annual MIPs until the mortgage reaches maturity or is terminated through one of the following actions:

- a. The mortgage is paid in full;
- b. A deed to the QPE is filed for record;
- c. An application for initial claim payment is received by the Commissioner; or
- d. The contract of insurance is otherwise terminated.

8. Cessation of Obligation to Pay MIP. The obligation to pay MIP will cease upon receipt by HUD of either of the following:

- a. A completed “Insurance Termination Request for Multifamily Mortgage” form HUD-9807. Requests for voluntary termination must be accompanied by the original credit instrument. When the termination is approved, the insurance endorsement will be cancelled.

and the credit instrument returned to the QPE. The instructions on form HUD-9807 are to be followed;

- b. The obligation to pay MIP will cease in the event a deed is filed for recordation, or an application for initial claim payment is received by the Commissioner; or
- c. If the Contract of Insurance is terminated by payment in full or is terminated by the QPE on a form prescribed by the Commissioner, after the date of first payment to principal, the Commissioner shall refund any unearned MIP paid for the period after the effective date of the termination of insurance. The unearned portion of MIP will be refunded to the QPE for credit to the mortgagor's account.

VIII. DEFAULT AND CLAIMS PROCEDURES

QPEs are responsible for filing notices of default and reinstatements, claims for insurance benefits including Partial Payment of Claims (PPC), issuing debentures, paying annual accrued interest on debentures, returning excess funds to Headquarters and submitting to Headquarters HUD's share of repayments. The Multifamily Asset and Counterparty Oversight Division in Headquarters is responsible for monitoring defaults, granting extensions, for reinstatements and notifying the Multifamily Claims Branch of these transactions. The Multifamily Claims Branch in Headquarters is responsible for computing and paying insurance benefits, holding debentures and tracking accrued interest received on debentures. The Multifamily General Ledger Accounting Branch and Multifamily Notes Servicing Branch in Headquarters is responsible for receiving and monitoring repayments on second mortgages.

A. Notice of Default and filing an insurance claim

1. Definition of Default.

- a. A monetary default exists when the mortgagor fails to make any payment due under the mortgage.
 - b. A covenant default exists when the mortgagor fails to perform any other covenant under the provision of the mortgage or the regulatory agreement, which is incorporated by reference in the mortgage. QPE becomes eligible for insurance benefits on the basis of a covenant default only after the QPE has accelerated the debt and the owner has failed to pay the full amount due, thus converting a covenant default into a monetary default.
2. Date of Default. For purposes of this Notice, the date of Default is:
 - a. The date of the first uncorrected failure to perform a mortgage covenant or obligation; or
 - b. The date of the first failure to make a monthly payment that is not covered by subsequent payments, when such subsequent payments are applied to the overdue monthly payments in the order in which they were due.
3. Notice of Default. If a Default (as defined in subparagraph (1) of this paragraph) continues for a period of 30 days, the QPE must notify the Commissioner within 10 days thereafter, unless the Default is cured within the 30-day period. Unless waived by the Commissioner, the QPE must submit this notice monthly, online using the Multifamily Delinquency and Default Report (MDDR), until the Default has been cured or the QPE has filed an application for an initial claim payment. In cases of mortgage acceleration, the mortgagee must first give Notice of the Default.
4. Timing of claim filing. Unless a written extension is granted by HUD, the QPE must file an application for initial claim payment (or, if appropriate, for partial claim payment) within 75 days from the Date of Default and may do so as early as the first day of the month following the month for which a payment was missed. Upon request of the QPE, HUD may extend, up to 180 days from the Date of Default, the deadline for filing a claim. In those cases where the QPE certifies that the

project owner is in the process of transacting a bond refunder, refinancing the mortgage, or changing the ownership for the purpose of curing the Default and bringing the mortgage current, HUD may extend the deadline for filing a claim beyond 180 days, not to exceed 360 days from the Date of Default.

B. Initial Claim Payments

1. Determination of Initial Claim amount.

a. The Initial Claim amount is based on the unpaid principal balance of the mortgage note as of the Date of Default, plus interest at the mortgage note rate from Date of Default to date of Initial Claim payment. The mortgage note interest component of the Initial Claim amount is subject to curtailment as provided in paragraph (2) of this section B(Initial Claim Payments).

b. HUD shall make an Initial Claim payment to the QPE or the custodian within 3 days of the filing of the Initial Claim that is equal to the Initial Claim amount, less any delinquent mortgage insurance premiums, late charges of 4 percent of the amount of the premium payment due, and interest at the rate prescribed by the Treasury Fiscal Requirements Manual.

c. The QPE must use the proceeds of the Initial Claim payment to retire any certificates of participation, bonds or any other financing mechanisms securing the mortgage within 30 days of the Initial Claim payment. Any excess funds resulting from such retirement or repayment shall be returned to HUD within 30 days of the retirement.

2. Curtailment of interest for late filings. In determining the mortgage note interest component of the initial claim amount, if the QPE fails to meet any of the requirements of this section within the specified time (including any granted extension of time), HUD shall curtail the accrual of mortgage note interest by the number of days by which the required action was late.

3. Method of payment. HUD shall pay the claim in cash.

C. Issuance of QPE Debenture

1. Condition to Initial Claim Payment. The QPE must issue an instrument in the form of a Debenture to HUD within 30 days of returning any excess funds resulting from retiring any bonds or financing mechanism securing the mortgage per paragraph (1)(c) of Section B (Initial Claims). If there are no excess funds to be returned to HUD, the QPE shall submit a letter stating that. The QPE Debenture shall meet the following requirements and shall be in a form that has been approved by HUD as part of the application approval process.
2. Term of QPE Debenture. The QPE Debenture shall be dated the same date that the Initial Claim payment is issued. The QPE Debenture shall have a term of five years in order to afford the mortgagor ample time to cure the Default or the QPE time to foreclose and/or resell the Project. HUD may provide a written extension of the five year term if the QPE certifies and provides documentation that the Project owner has filed bankruptcy and the QPE is taking action to have the project discharged from the bankruptcy. The QPE Debenture shall, during this extended period, continue to bear interest as described below at HUD's published debenture rate at the earlier of initial endorsement or final endorsement. Interest shall be due and payable annually on the anniversary date of the Initial Claim payment. Interest is due on the full face amount of the QPE Debenture through the term of the QPE Debenture or through the date an application for Final Claim payment is received by the Commissioner.
3. QPE Debenture amount.
 - a. The QPE Debenture shall be for the full Initial Claim amount as determined under paragraph (1)(a) of Section B (Initial Claims) (minus any excess funds returned to HUD under paragraph (1)(c) of Section B (Initial Claims)).
 - b. The full amount of the QPE Debenture shall be payable to HUD upon maturity, unless the

QPE Debenture is canceled because of the Final Claim settlement under Section K (Final Claim Settlement and QPE Debenture).

4. QPE Debenture interest rate. The QPE Debenture shall bear interest at HUD's published debenture rate at the earlier of initial endorsement or final endorsement. Interest shall be due and payable annually on the anniversary date of the initial claim payment and on the date of redemption when redeemed or canceled before an anniversary date. Interest shall be computed on the full face amount of the QPE Debenture through the term of the QPE Debenture.
5. Form of QPE Debenture. The QPE Debenture should follow the standard form of a State/Municipal Debenture issued under the Uniform Commercial Code, where applicable, and shall be supported by the full faith and credit of the QPE.
6. Debenture registration. Unless otherwise required by law, including State or local laws, or other governing bodies, HUD will not require the QPE Debenture to be "Registered" (with the Securities and Exchange Commission) as it is a direct, or private, placement, and not a public offering, that is supported by the full faith and credit of the QPE.

Debentures shall be sent to:

U.S. Department of Housing and Urban Development\
Multifamily Claims Branch
P.O. Box 44003
Washington, DC 20026

Accrued interest on the debenture and the full amount of the matured Debenture are to be sent to the address stated above. The QPE certifies and provides documentation of bankruptcy actions filed by the project owner and certifies the QPE is taking action to have project discharged from bankruptcy. The QPE must immediately notify the Multifamily Insurance Operations Branch, the local HUD

Counsel, and the Multifamily Asset and Counterparty Oversight Division of all notifications and bankruptcies.

D. Foreclosure and Acquisition

The QPE is not required to foreclose the insured mortgage. It may accept a deed-in-lieu of foreclosure.

E. Appraisals

Where actions taken or caused to be taken by the QPE have the effect of the recovery of less than the face amount of the QPE Debenture held by HUD, an appraisal should be made to determine the value of the project. The appraisal should assume a willing buyer and a willing seller. The appraisal must be done within the 45-day period immediately preceding the date when the QPE files an application for Final Claim settlement. If at the time of Final Claim settlement the QPE has not sold the project, an appraisal should be made to determine the value of the project at its highest and best use.

F. Application for final claim settlement

The QPE shall file an application for Final Claim settlement in accordance with the Commissioner's administrative procedures not later than 30 days after any of the following:

1. Sale of the property after foreclosure or after acquisition by deed-in-lieu of foreclosure; or
2. Expiration of the term of the QPE Debenture.

G. Determining the amount of loss

The amount of the total loss to be shared by HUD and the QPE is equal to:

1. The amount of the Initial Claim payment;
2. Plus all items set forth in paragraph H below; and
3. Less all items set forth in paragraph I below.

H. Items included in total loss

In computing the total loss, the following items are added to the amount described in Section G (Determining the amount of loss):

1. The amount of all payments that the QPE made from its own funds and not from Project income for:
 - a. Taxes, special assessments, and water bills that are liens before the Mortgage; and
 - b. Fire and hazard insurance on the property.
2. A reasonable amount of acquisition costs actually paid by the QPE. These costs may not include loss or damage resulting from the invalidity or unenforceability of the mortgage lien or the un-marketability of the mortgagor's title.
3. Reasonable payments that the QPE made from its own funds and not from project income for:
 - a. Preservation, operation and maintenance of the property;
 - b. Repairs necessary to meet the requirements of local laws;
 - c. Expenses in connection with the sale of property; and
 - d. Bankruptcy expenses approved by the Office of General Counsel
 - e. The amount of QPE Debenture interest paid by the QPE to HUD.

I. Items deducted from total loss

In computing insurance benefits, the following items are deducted from the amounts described in 1 and 2 of Section G (Determining the amount of loss):

1. All amounts received by the QPE on account of the mortgage after the Date of Default;
2. All cash, and/or funds related to the mortgaged property, including deposits and escrows made for the account of the mortgagor that the QPE holds (or to which it is entitled);
3. The amount of any undrawn balance under a letter of credit that the QPE accepted in lieu of a

cash deposit for an escrow agreement;

4. Any net income from the mortgaged property/project that the QPE received after the Date of Default;

5. The proceeds from the sale of the project or the appraised value of the project as provided in paragraph E above as follows:

a. If the QPE disposes of the project through a negotiated sale, the amount deducted shall be the higher of the sales price or the appraised value;

b. If the QPE disposes of the project through a competitive bid procedure approved by the Commissioner, the amount deducted shall be the sales price, even if it is lower than the appraised value;

c. If the QPE has not disposed of the project within 5 years from the date of issuance of the QPE Debentures (unless an extension has been granted pursuant to paragraph 3 above, the amount deducted shall be the appraised value.

6. Any and all claims that the QPE has acquired in connection with the acquisition and sale of the property. Claims include but are not limited to returned premiums from canceled insurance policies, interest on investments of reserve for replacement funds, tax refunds, refunds of deposits left with utility companies, and amounts received as proceeds of a receivership.

7. The amount of daily QPE Debenture interest accrued but not paid from the anniversary date of the last QPE Debenture interest payment to the date an application for Final Claim payment is received by the Commissioner.

J. Determining share of loss

The total loss computed in paragraph G above shall be shared by HUD and the QPE in accordance with their respective percentage of risk as specified in the note and the addendum to the

RSA between HUD and the QPE.

K. Final claim Settlement and QPE Debenture redemption

1. Final Claim payment. If the Initial Claim amount, as determined under paragraph (1)(a) of Section B (Initial Claim Payments) above, is less than HUD's share of the loss, HUD shall make a Final Claim payment to the QPE that is equal to the difference between HUD's share of the loss and the Initial Claim amount and shall return the QPE Debenture to the QPE for cancellation.
2. QPE reimbursement payment. If the Initial Claim amount, as determined under paragraph 1 of Section B (Initial Claim Payments), is more than HUD's share of the loss, the QPE shall, within 30 days of notification by HUD of the amount due, remit to HUD an amount that is equal to the difference between the Initial Claim amount and HUD's share of the loss. The funds must be remitted in a manner prescribed in the Commissioner's administrative procedures. The QPE Debenture will be considered redeemed upon receipt of the cash payment. A 5 percent penalty will be charged and interest at the debenture rate will begin to accrue if the cash payment is not received within the prescribed period.
3. Losses. Losses sustained as a consequence of the (sole) negligence of a QPE (*e.g.*, failure to acquire adequate hazard insurance where such insurance is available) shall be the sole obligation of the QPE, notwithstanding the risk apportionment otherwise agreed to by HUD and the QPE.
4. Supplemental claim. Any supplemental claim must be filed within one year from date of Final Claim settlement.

L. Recovery of costs after Final Claim Settlement

If, after Final Claim Settlement, the QPE recovers additional sums as the result of the sale of the project or otherwise, the total amount of such recovery shall be shared by HUD and the QPE in accordance with the prescribed percentage of shared risk.

IX. EXHIBITS

Basic Underwriting Requirements for Small Building Initiative Loans

Exhibit 1: Basic Underwriting Requirements for Small Buildings Initiative Loans

1. The mortgage loan shall have a fixed interest rate.
2. The mortgage loan shall have a loan to value ratio of no more than 90%.
3. The mortgage shall have a debt service coverage ratio of no less than 1.15:1.
4. The mortgage loan may be fully amortizing with a term of not more than forty (40) years; or
5. The mortgage loan may require a balloon payment of the outstanding principal no sooner than the end of year fifteen calculated on a term of no more than thirty (30) years.
6. The mortgage must be recorded.
7. The mortgage must be on real property.
8. The eligible project must either be owned in fee simple by the mortgagor or held pursuant to a lease in which the lease, at origination, is not less than 40 years and at least 10 years longer than the amortization period applicable to the mortgage loan.
9. The mortgage shall constitute a single first lien and shall be free of all liens other than the lien in favor of the QPE and such subordinate liens approved by the QPE.
10. The mortgage shall contain an affordability restriction lasting throughout the term of the loan.
11. The mortgage shall require the mortgagor to comply with: the Fair Housing Act, as implemented by 24 C.F.R. part 100; Executive Order 11063, as amended, and implemented by 24 C.F.R. part 107; and other applicable State and local fair housing and equal opportunity laws.
12. The mortgage shall require that the mortgagor be a single-asset mortgagor unless this requirement is waived in writing by the QPE.

13. The mortgage loan shall not have an uncured payment default or a performance default when the QPE submits a Risk Sharing Request with respect to such mortgage loan.

14. The QPE shall commission a CNA to identify all capital needs so they can be adequately addressed in the rehabilitation and/or reserve requirements.