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DEPARTMENT OF AGRICULTURE

Rural Housing Service

7 CFR Part 3550

RIN 0575-AC81

Direct Single Family Housing Loans and Grants

AGENCY: Rural Housing Service, USDA.

ACTION: Final rule.

SUMMARY: Through this action, the Rural Housing Service (RHS) amends its regulations for the Direct Single Family Housing Loans by reinstating language in the Single Family Housing (SFH) recapture regulation to enable full repayment of the entire subsidy in event of foreclosure or deed-in-lieu of foreclosure (voluntary conveyance).

This action clarifies that in the event of foreclosure or deed-in-lieu of foreclosure (voluntary conveyance) the RHS will recapture the full subsidy from the value of the property.

DATES: Effective: [INSERT DATE 30 DAYS FROM DATE OF PUBLICATION IN THE FEDERAL REGISTER].

FOR FURTHER INFORMATION CONTACT: Michael S. Feinberg, Chief, Loan Origination Branch, Single Family Housing Direct Loan Division, Rural Housing Service, Stop 0783, 1400 Independence Avenue SW, Washington, DC 20250-0783, Telephone: 202-720-1474.

SUPPLEMENTARY INFORMATION:

Classification

This rule has been determined to be not significant and was not reviewed by the Office of Management and Budget (OMB) under Executive Order 12866.

Paperwork Reduction Act of 1995

There are no new reporting and recordkeeping requirements associated with this rule.

E-Government Act Compliance

The RHS is committed to complying with the E-Government Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

Civil Justice Reform

This rule has been reviewed under Executive Order 12988, Civil Justice Reform. In accordance with that Executive Order: (1) All State and local laws and regulations that are in conflict with this rule will be preempted; (2) No retroactive effect will be given to this rule; and (3) Administrative proceedings in accordance with the regulations of the National Appeals Division of USDA at 7 CFR part 11 must be exhausted before bringing suit in court challenging action taken under this rule unless those regulations specifically allow bringing suit at an earlier time.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), 2 U.S.C. 1501 *et seq.*, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, RHS generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with "Federal mandates" that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector, of \$100 million or more in any one year. When such a statement is needed for a rule, section 205 of the UMRA generally requires RHS to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective or least burdensome alternative that achieves the objectives of the rule. This rule contains no Federal mandates (under the regulatory provisions of Title II of the UMRA) for State, local, and tribal Governments or the private sector. Therefore, this rule is not subject to the requirements of sections 202 and 205 of the UMRA.

Programs Affected

The programs affected by this proposed rule are 10.410, Low to Moderate Income Housing Loans, and 10.417, Very Low-Income Housing Repair Loans and Grants.

Intergovernmental Consultation

For the reasons set forth in the final rule published at 7 CFR part 3015, subpart V, and the related notice (48 FR 29115), these programs are not subject to Executive Order 12372, which requires intergovernmental consultation with State and local officials.

Environmental Impact Statement

This document has been reviewed in accordance with 7 CFR part 1940, subpart G, "Environmental Program." It is the determination of RHS that this action does not constitute a major Federal action significantly affecting the quality of the human environment, and in accordance with the National Environmental Policy Act of 1969, Pub. L. 91-190, an Environmental Impact Statement is not required.

Regulatory Flexibility Act

This rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act (5 U.S.C. 601-612). The undersigned has determined and certified by signature of this document that this rule will not have a significant economic impact on a substantial number of small entities. This rule reinstates a requirement on Agency applicants and borrowers; however, the requirement of full subsidy recapture in event of foreclosure or voluntary conveyance will apply solely to the individual applicants and borrowers of Section 502 Direct Single Family Housing financing and will not apply to small entities. There will be no significant information collection or regulatory requirements imposed on small entities under this rule.

Federalism

The policies contained in this rule do not have any substantial direct effect on States, the relationship between the National Government and the States, or on the distribution of power and responsibilities among the various levels of government. Nor does this rule

impose substantial direct compliance costs on State and local Governments. Therefore, consultation with the States is not required.

Background

In the event of a foreclosure or deed in lieu of foreclosure (voluntary conveyance), the original recapture regulation promulgated on October 1, 1979, (7 CFR part 1951, subpart I (1980)) provided for recapture of the full amount of subsidy granted in determining the balance owed. However, when the Section 502 SFH direct loan program was restructured on November 22, 1996, the revised recapture regulation, 7 CFR 3550.162, omitted this provision. Therefore, because of the omission of the critical language in the regulation, full recovery is not currently supported by regulatory authority.

Foreclosure or deed in lieu of foreclosure is a last resort to protect the Government's interest after all other servicing actions have failed. Recovery of some or the entire payment subsidy provided to direct single family housing borrowers or "recapture" is provided for by statute in 42 U.S.C. 1490a (a)(1)(D). The statute gives the Secretary broad discretion in determining the amount of the subsidy recapture.

A proposed rule was published on March 5, 2010, [75 FR 10194 – 10195] to provide clear regulatory authority in 7 CFR part 3550 for full recovery of the payment assistance subsidy that the borrower has received in the event of foreclosure or deed in lieu of foreclosure. This final rule further clarifies the subsidy repayment requirement in event of foreclosure or deed in lieu of foreclosure by restoring the original regulatory authority

and policy of full recovery of the subsidy in these situations in 7 CFR 3550.162(b)(2). The Subsidy Repayment Agreement (Form RD 3550-12) signed by the borrower has been revised accordingly to reflect the language of the regulation.

This rule also clarifies in 7 CFR 3550.162(b)(2) that the borrower will not be personally liable for any deficiency in repayment of the full subsidy to the Agency and the Agency will not seek to recover unpaid subsidy from assets of the borrower other than the property which was security for the loan. This policy was stated in the original recapture regulation promulgated on October 1, 1979, but unintentionally omitted from 7 CFR 3550.162 when the program was restructured in 1996.

No comments were received on the Proposed Rule; however, the Agency made a several changes to the proposed rule for organization and clarification purposes. The Agency revised paragraph (a) to clarify that “payment subsidy” includes subsidy from the former interest credit program, and that foreclosure and deed in lieu of foreclosure are examples of situations in which “the borrower transfers title or ceases to occupy the property.” The Agency also clarified that recapture would include the amount of principal reduction attributed to subsidy (PRAS), except in cases of foreclosure and deed in lieu of foreclosure. PRAS would have benefitted borrowers with loans receiving interest credit subsidy between October 1, 1979 and December 31, 1989. This limited recapture of PRAS is consistent with the Subsidy Repayment Agreement used during that time.

The Agency also moved some language from proposed paragraph (a) to paragraph (b)(2) to more clearly distinguish its recapture procedure for foreclosure and deed in lieu of foreclosure from other situations. The Agency further explained its current policy on how liquidation proceeds are to be applied to a borrower's debt to make clear that no preference is made to recover subsidy from security proceeds.

Subparagraph (b)(1)(General) was clarified for non-foreclosure/deed in lieu of foreclosure cases, to reference the calculation for value appreciation under the applicable Subsidy Repayment Agreement (SRA). These agreements have been revised over the years and will be enforced according to their terms and current regulations to the extent not inconsistent with the applicable agreements. The paragraph also was clarified to specify current Agency procedure that upon Agency request borrowers will provide property appraisals, including those for any capital improvements, or arm's length sales contracts to establish market value for determining value appreciation. Agency appraisal standards are found in 7 CFR 3550.62.

Existing policies for deferral of recapture and recapture when the loan is assumed by a third party have been reinserted as paragraphs (c) and (d) of 7 CFR 3550.162. A discount is available when the borrower timely pays recapture at settlement or upon notice instead of deferring payment until the property is sold or vacated. This discount amount is consistent with current 25% discount policy under the Subsidy Repayment Agreement and handbook procedures. No change in policy was intended in the proposed rule on these issues.

A cross-reference to 7 CFR 3550.162 was added to 3550.202(b) concerning the acceleration of past due accounts.

List of Subjects in 7 CFR Part 3550

Accounting, Housing, Loan programs- Housing and community development, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, chapter XXXV, Title 7 of the Code of Federal Regulations, is amended as follows:

PART 3550 – DIRECT SINGLE FAMILY HOUSING LOANS AND GRANTS

1. The authority citation for part 3550 continues to read as follows:

Authority: 5 U.S.C. 301; 42 U.S.C. 1480.

Subpart D – Regular Servicing

2. Section 3550.162 is revised to read as follows:

§ 3550.162 Recapture.

(a) *Recapture policy.* Borrowers with loans approved or assumed on or after October 1, 1979, will be required to repay subsidy amounts received through payment subsidy (including the former interest credit program) or deferred mortgage assistance in accordance with paragraph (b) of this section. Amounts to be recaptured are due and

payable when the borrower transfers title or ceases to occupy the property, including but not limited to, in the event of foreclosure or deed in lieu of foreclosure. Such recapture will include the amount of principal reduction attributed to subsidy (for loans subject to recapture that were approved, and received interest credit, between October 1, 1979, and December 31, 1989), except in cases of foreclosure and deed in lieu of foreclosure.

(b) *Amount to be recaptured.* (1) *General.* The amount to be recaptured is the amount of principal reduction attributed to subsidy plus the lesser of:

(i) The amount of subsidy received; or

(ii) A portion of the value appreciation of the property subject to recapture. In order for value appreciation to be calculated, the borrower will provide a current appraisal, including an appraisal for any capital improvements, or arm's length sales contract as evidence of market value upon Agency request. Appraisals must meet Agency standards under § 3550.62.

(2) *Foreclosure or deed in lieu of foreclosure.* Notwithstanding paragraph (b)(1) of this section, the amount to be recaptured in a foreclosure or deed in lieu of foreclosure is the amount of subsidy received, not including any principal reduction attributed to subsidy. Foreclosure actions will seek to recover such amounts only from the proceeds of the property. Liquidation proceeds (in the case of foreclosure) or the net recovery value (in the case of deed in lieu of foreclosure) will be applied or credited to the borrower's debt in accordance with the security agreement in the following order:

(i) Recoverable costs (e.g. protective advances, foreclosure costs, late charges).

(ii) Accrued interest.

(iii) Principal.

(iv) Subsidy.

(3) *Value appreciation.* The value appreciation of property with a cross-collateralized loan is based on the market value of the dwelling and lot. If located on a farm, the lot size would be a typical lot for a single family housing property.

(4) *Interest* reduced from the promissory note rate to six percent under the Servicemembers Civil Relief Act (SCRA) is not subject to recapture.

(c) *Deferral of recapture.* If the borrower refinances or otherwise pays in full without transfer of title and continues to occupy the property, the amount of recapture will be calculated in accordance with paragraph (a) of this section but payment of recapture may be deferred, interest free, until the property is sold or vacated. If the recapture amount is deferred, the Agency mortgage can be subordinated when in the Government's best interest but will not be released nor the promissory note satisfied until the Agency is paid in full. In situations where deferral of recapture is an option, recapture will be discounted if paid in full at the time of settlement or timely paid after Agency notification to the borrower that recapture is due.

(d) *Assumed loans.* (1) When a loan subject to recapture is assumed under new rates and terms, the recapture amount may be paid in full by the seller or included in the principal amount assumed by the buyer.

(2) When a loan is assumed under the same rates and terms as the original promissory note, recapture amounts will not be due. When the new borrower transfers title or ceases

to occupy the property, all subsidy subject to recapture before and after the assumption is due.

(3) When a borrower has deferred payment of recapture amounts, the deferred recapture amount may be included in the principal amount of the new loan.

Subpart E – Special Servicing

3. Section 3550.202 is amended by adding paragraph (b)(3) to read as follows:

§ 3550.202 Past due accounts.

* * * * *

(b) * * *

(3) *Subsidy recapture.* Acceleration under this section will take into account any subsidy recapture due under § 3550.162.

Tammye Treviño
Administrator
Rural Housing Service

January 16, 2012
Date

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