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DEPARTMENT OF AGRICULTURE

Rural Housing Service

7 CFR Part 3550

[Docket No. RHS-19-SFH-0020]

RIN 0575-AD14

Single Family Housing Direct Loan and Grant Programs

AGENCY: Rural Housing Service, USDA.

ACTION: Proposed rule.

SUMMARY: Through this proposed rule, the Rural Housing Service (RHS or Agency) is proposing to amend its regulations to update and improve the direct Single-Family Housing (SFH) loans and grants programs. The proposed changes would increase program flexibility, allow more borrowers to access affordable loans, better align the programs with best practices, and enable the programs to be more responsive to economic conditions and trends.

DATES: Comments on the proposed rule must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments to this rule through the Federal eRulemaking Portal: Go to <http://www.regulations.gov> and, in the lower "Search Regulations and Federal Actions" box, select "Rural Housing Service" from the agency drop-down menu, then click on "Submit." In the Docket ID column, select RHS-19-SFH-0020 to submit or view public comments and to view supporting and related materials available electronically.

Information on using Regulations.gov, including instructions for accessing documents, submitting comments, and viewing the docket after the close of the comment period, is available through the site's "User Tips" link.

All comments will be available for public inspection online at the Federal eRulemaking Portal (<http://www.regulations.gov>).

FOR FURTHER INFORMATION CONTACT: Andrea Birmingham, Finance and Loan Analyst, Single Family Housing Direct Loan Division, USDA Rural Development, STOP 0783, 1400 Independence Ave SW., Washington, DC 20250-0783, Telephone:

(202) 720-1489. E-mail: andrea.birmingham@usda.gov.

SUPPLEMENTARY INFORMATION:

Background and Proposed Changes

In order to improve the delivery of the SFH loan programs and to promote consistency among the programs when appropriate, RHS is proposing to amend its regulations at 7 CFR part 3550 for the direct SFH loan and grant programs by:

(1) Revising and adding specific definitions to § 3550.10:

a. Revise the definition of modest housing, which currently prohibits in-ground swimming pools. The revised definition would allow for the financing of existing modest homes with pools. Existing housing stocks are very limited in many rural areas, and this is an unnecessary prohibition to homeownership when an otherwise modest and affordable home is typical for the area but cannot be financed because of a pool. The proposed change promotes a degree of consistency with the SFH guaranteed loan program, which does not prohibit in-ground swimming pools. In-ground pools with new construction, or with dwellings that are purchased new, would still be prohibited.

b. Remove the definition of national average area loan limit. This removal would complement changes proposed to § 3550.52(d)(6) in a separate rulemaking (83 FR 44504 (August 31, 2018)).

c. Revise the definition of the PITI ratio to include homeowner's association dues and other recurring, housing-related assessments. The change would reduce the risk of financing a property which may not be truly affordable to the homeowner. This risk occurs because of a PITI ratio which may be too low when recurring housing related costs such as mandatory homeowner's association dues and land lease payments are not taken into consideration during underwriting. This change would result in more accurately calculating the front end, PITI ratio for housing related costs; and in turn, calculating a more accurate Total Debt ratio on the back end.

Calculating more accurate ratios will help ensure a loan amount is approved at an affordable level for the borrower.

d. Revise the veterans' preference definition to remove obsolete information and streamline the definition by citing the definition of a veteran or a family member of a deceased service member in 42 U.S.C. 1477.

e. Add definition for principal residence. The definition would align with that used in the SFH guaranteed loan program and the mortgage industry.

(2) Changing references § 3550.11(a) and (b) to "homeowner education" to "homeownership education" for consistency, and removing the requirement placed on State Directors to update the list of homeownership education providers annually. The Agency proposes to require State Directors to update the list on an as-needed basis, but no less frequently than every three years. The proposed rule also specifies that the Agency would determine preferences for education format (i.e. online, in-person, telephone) based on effectiveness, availability and industry practice. The Agency would publish the education format preferences in a publicly available format, such as the program handbook. These changes would allow the Agency to be more responsive to changes in homeowner education course delivery and availability.

(3) Revising § 3550.52(a) to allow a new borrower to use new loan funds to purchase a dwelling from an existing RHS borrower. The current regulation requires the new borrower to assume the existing loan. Under the proposed revision, the Agency would determine if these transactions will be financed using an assumption of the existing RHS

indebtedness or new loan funds, depending on funding levels as well as program goals and needs. This revision would allow the Agency to responsibly, effectively, and fully utilize funds appropriated by Congress without the additional steps required to process and close a loan assumption and subsequent new loan, thereby reducing loan application processing times.

(4) Revising the packaging fee requirements in § 3550.52(d)(6) to allow the Agency more flexibility to specify packaging fees for the non-certified loan application process, and to ensure non-certified packaging fees reflect the level of service provided and the prevailing cost to provide the service.

For the non-certified loan packaging process, the current fee may not exceed \$350, but this limit would be revised as it does not necessarily reflect the time a non-certified loan packager invests in the packaging process. Under the proposed revision, the packaging fees for the non-certified loan packaging process may not exceed a limit determined by the Agency and is no greater than one percent of the national average area loan limit. The Agency will determine the exact limit within the one percent threshold based on factors such as the level of service provided and the prevailing cost to provide the service and will publish

the exact limit in a publicly available format such as the program handbook.

This rule also proposes to amend this paragraph to remove the language regarding a preliminary eligibility determination to streamline the process, and to clarify that the packaging fee is paid only if the loan closes.

(5) Revising § 3550.53(c) and removing (c)(1) through (3) to remove the overly restrictive primary residence requirements for military personnel and students. These requirements prohibit approving loans for active duty military applicants, unless they will be discharged within a reasonable period; and for full time students unless there are reasonable prospects that employment will be available in the area after graduation. Active duty military personnel and full-time students provide valuable service experience, education, and civic and financial contributions to rural areas. Providing these applicants with more opportunity to own modest, decent, safe, and sanitary homes in rural areas would strengthen the fabric of those communities. In addition, removing this overly restrictive language will improve consistency with other Federal housing programs such as the U.S. Department of Housing and Urban Development and the U.S. Department of Veterans Affairs.

(6) Revising § 3550.53(g) and removing § 3550.53(g) (1) through (5) to include the new definition of PITI for clarity; and to revise repayment ability ratio thresholds to use the same ratios for both low- and very-low income applicants (which will help ensure equal treatment of applicants across the income categories and improve the marketability of the program) and to increase the ratios by a small percentage to reflect common industry tolerances. This change, in conjunction with automated underwriting technology, will address risk layers and reduce the frequent requests for PITI ratio waivers due to compensating factors.

(7) Replacing "homeowner" with "homeownership" in § 3550.53(i) for consistency within part 3550.

(8) Revising § 3550.55(c) introductory text and (c) (4) and (5) so that application processing priorities are applied on a regular basis, and not just during periods of insufficient funding. Current regulations only trigger priorities in application processing when funding is insufficient. However, applying these priorities on a regular basis, not just during insufficient funding, will provide clear processing priorities for RHS staff. In the case of applications with equivalent priority status that

are received on the same day, preference will be extended to applicants qualifying for a veterans' preference.

This proposed change recognizes that RHS has limited staff resources and that complete applications need to be prioritized for processing, as well as for funding when funds are limited. While the goal is to determine an applicant's eligibility for the program within 30 days of receiving a complete application regardless of their priority ranking and the availability of funds, the priority ranking will direct Agency staff how to prioritize their work processes and better meet urgent needs. The proposed amendment would also give fourth priority to applications submitted via an intermediary through the certified application packaging process outlined in § 3550.75. Currently, RHS may temporarily classify these applications as fourth priority when determined appropriate—the proposed change would make the fourth priority status permanent and applicable at all times. The change in priority does not impact the priority of any other category and will recognize and encourage the participation and interest of intermediaries in the direct SFH program. Intermediaries are valuable to the program by helping attract program applicants, training certified

packagers, and performing quality assurance reviews of applications.

Other priorities remain unchanged including existing customers who request subsequent loans to correct health and safety hazards, loans related to the sale of REO property or ownership transfer of an existing RHS financed property, hardships including applicants living in deficient housing for more than six months, homeowners in danger of losing property through foreclosure, applicants constructing dwellings in an approved self-help project, and applicants obtaining other funds in an approved leveraging proposal. Veterans' preference also remains a priority in accordance with 42 U.S.C. 1477. To further emphasize these priorities, the Agency proposes to also make funding available in accordance with same priorities as application processing.

(9) Revising § 3550.56(b)(3) to remove the requirement that the value of the site must not exceed 30 percent of the "as improved" market value of the property. The site value is not necessarily an indicator of whether the property is modest. Other Agency requirements including area loan limits, appraisals, purchase agreements, and construction contracts are better indicators of whether the property is considered modest.

Site values in high cost areas typically exceed the 30 percent threshold even in rural communities, and the frequent requests for waivers of this requirement impose an unnecessary administrative burden. This change would also be consistent with the guaranteed SFH loan program, which has no site value limitation.

(10) Amending § 3550.57(a) to remove the reference to in-ground swimming pools for existing housing under the Section 502 program, to align the paragraph with the revised modest housing definition in § 3550.10 of this proposed rule.

(11) Revising § 3550.59(a)(2) to remove the requirement that the amount of a junior lien, when it is a grant or a forgivable affordable housing product, may not exceed the market value by more than 5 percent (i.e. up to a 105% loan to value ratio). This is an overly restrictive requirement as it relates to grants and forgivable affordable housing products as these products often partially or completely cover the cost of rehabilitation to make the dwelling decent, safe, and sanitary, and a higher loan to value ratio may be tolerated in these instances.

Beginning in FY 2016, RHS initiated a pilot in a limited number of states to allow the State Office to approve leveraging arrangements where the total loan-to-

value was more than the 105% limitation identified in § 3550.59(a)(2), provided:

- RHS is in the senior lien position and the RHS loan is fully secured (with allowable exceptions for the tax service fee, appraisal fee, homebuyer education and initial escrow for taxes and insurance);

- The junior lien is for an authorized loan purpose identified in § 3550.52;

- The junior lien involves a grant or forgivable affordable housing product; and

- The grant or forgivable affordable housing product comes from a recognized grant source such as a Community Development Block Grant or a HOME Investment Partnerships Program (HOME).

The pilot has been successful because it has:

- Empowered the selected State Offices to make timely decisions on loans with junior liens involving a grant or forgivable affordable housing product, and gave the junior lien holder the discretion to determine a total loan-to-value that could be supported within their own program requirements;

- Generally improved an area's rural housing stock since the grants and forgivable affordable housing products

are frequently used for rehabilitation work where the rehab cost is more than the enhanced value;

- Promoted consistency with the guaranteed SFH loan program, which states that junior liens by other parties are permitted if the junior liens do not adversely affect repayment ability or the security for the guaranteed loan; and

- Increased partnerships with nonprofits.

The proposed amendment would codify the positive aspects of the pilot so that the advantages will apply program wide.

(12) Revising § 3550.67(c) to allow more small Section 502 direct loans to be repaid in periods of up to 10 years. The current regulation states that only loans of \$2,500 or less must not have a repayment period exceeding 10 years. In practice, loans of less than \$7,500 are generally termed for 10 years or less so that the loan can be unsecured (i.e. no mortgage or deed of trust is required) in accordance with the program's guidance.

This revision will provide the Agency flexibility in setting the dollar threshold for smaller loans which may have a repayment period that does not exceed 10 years. This threshold will be determined by the Agency and published in a publicly available format such as the

program handbook and will not exceed ten percent of the national average area loan limit. The Agency will determine the threshold based on factors such as the Agency's level of tolerance for unsecured loans and the performance and collection of unsecured loans in the Agency's portfolio.

(13) Removing the language in § 3550.103(e) regarding a waiver of the requirement that applicants must be unable to obtain financial assistance at reasonable terms and conditions from non-RHS credit or grant sources and lack the personal resources to meet their needs. The regulation currently provides that this requirement may be waived if the household is experiencing medical expenses more than three percent of the household's income. The revision would remove the medical expense and waiver language. The authority to waive regulations on a case-by-case basis already exists in § 3550.8, making the medical expense and waiver language in § 3550.103(e) unnecessary. Furthermore, limiting the waiver of the requirement to only those instances in which medical expenses exceed 3 percent of the household's income is overly restrictive.

(14) Revising § 3550.104(c) to replace "veterans preference" with "veterans' preference." This is a grammatical correction only.

(15) Revising § 3550.106(a) to remove the reference to in-ground swimming pools for the Section 504 program, to align the paragraph with the revised modest housing definition in § 3550.10 of this proposed rule.

(16) Revising § 3550.108(b)(1) to modify the requirement for title insurance and a closing agent for certain secured Section 504 loans of \$7,500 and greater. Currently, Section 504 loans less than \$7,500 may be closed by the Agency without title insurance and a closing agent; however, loans of \$7,500 and greater require title insurance and must be closed by a closing agent. The cost for title insurance and a closing agent can be unaffordable for very-low income borrowers with loans of \$7,500 and greater or can potentially decrease the amount of loan funds available for needed repairs or improvements. This revision would remove the specific dollar threshold for loans which would require title insurance and closing agent. Loans where the total section 504 indebtedness does not exceed an amount determined by the Agency, but no greater than twenty percent of the national average area loan limit, may be closed by the Agency without title insurance or a closing agent. The Agency will determine the maximum amount based on factors such as average costs for title insurance and closing agents compared to average

housing repair costs and publish the specific threshold in a publicly available format such as the program handbook. This revision would significantly reduce loan closing costs incurred by the borrowers, by allowing more loans to be closed by the Rural Development office. This revision would also allow for responsiveness and adjustments based on inflationary changes.

(17) Revising § 3550.112(a) to revise the Section 504 maximum loan amount of \$20,000, so that the sum of all outstanding section 504 loans to one borrower and for one dwelling may not exceed an amount determined by the Agency, but not greater than twenty percent of the national average area loan limit, and published in a publicly available format, such as the program handbook. The Agency will determine the maximum amount based on factors such as average loan amount and repair costs. A corresponding change will also be made to § 3550.112(a)(1) to address maximum loan amounts for transferees who assume Section 504 loans and wish to obtain a subsequent loan. The revision allows the Agency greater responsiveness and flexibility to address changes to average repair costs.

(18) Removing the lifetime maximum assistance of \$7,500 for a Section 504 grant and allowing the Agency to

apply a lifetime grant limit to any one household or one dwelling.

(19) Revising the Section 504 loan term requirements to specify that the loan term will be 20 years.

(20) Revising the recapture requirements in § 3550.162(b) to specify when Principal Reduction Attributable to Subsidy (PRAS) is, or is not, collected.

The direct loan program provides payment assistance (subsidy), which may include PRAS, to help borrowers meet their monthly mortgage loan obligations. At time of loan payoff), borrowers are required to repay all or a portion of the subsidy they received over the life of the loan. This is known as subsidy recapture. The amount of subsidy recapture to be repaid is based on a calculation that determines the amount of value appreciation (equity) the borrower has in the property at time of payoff. The proposed changes to the regulation specify when PRAS is collected. In cases where the borrower has no equity in the property based on the recapture calculation, PRAS will not be not collected. There are no changes to the current subsidy recapture calculation.

(21) Revising the payment moratorium requirements in § 3550.207 to require reamortization of each loan coming off a moratorium.

Currently, the regulation stipulates that at the end of a moratorium borrowers are to be provided a re-amortization if the Agency determines they can resume making scheduled payments, based on financial information provided by the borrower. Often these borrowers lack demonstrable repayment ability for the new installment, which then requires the Agency to liquidate the account. However, it should not be unexpected that a borrower may have difficulty demonstrating repayment ability at the end of a moratorium. The very purpose of the moratorium is to provide temporary payment relief to borrowers who have experienced circumstances beyond their control such as the loss of at least 20 percent of their income, unexpected expenses from illness, injury, death in the family, etc.

In July 2010, due to the recession, the Administrator of RHS issued a decision memorandum approving the re-amortization of all accounts following a moratorium; this decision has been supported by subsequent Administrators. Historical data has shown that borrowers whose loans are re-amortized after a moratorium, regardless of repayment ability, have no greater risk of becoming delinquent when compared to non-moratorium borrowers whose loans were re-amortized.

When comparing the borrower's repayment history 18 months after the moratorium/re-amortization, 81.5 percent of the borrowers made their required monthly payment and avoided foreclosure, making this the best option for the borrower and the Agency. Whereas, if the borrower's repayment ability would have been considered, a large percentage of these successful borrowers would have lost their home without being given a chance to demonstrate their ability to repay their mortgage.

This revision would require reamortization after a moratorium regardless of repayment ability, which would reduce foreclosures and better serve borrowers.

The Agency is also clarifying that all or part of the interest accrued during the moratorium may be forgiven in an amount that balances affordability to the borrower and serving the best interest of the government.

(22) Revising § 3550.251(c) and (d) to remove obsolete references and clarify the process and priorities in the sale or lease of Real Estate Owned (REO) properties. The revision would also clarify the sale or lease process and reservation periods for priority buyers to comply with 42 U.S.C. 11408a.

Under 42 U.S.C. 11408a, RHS must lease or sell program and nonprogram inventory properties public agencies and

nonprofits to provide transitional housing and to provide turnkey housing for tenants of such transitional housing and for eligible families. However, first priority is the sale of REO properties to Section 502 borrowers.

The proposed changes would further align § 3550.251(c) and (d) with 42 U.S.C. 11408a concerning the priority of the sale or lease of REO properties to eligible borrowers and to nonprofit organizations or public bodies providing transitional housing.

The proposed action will incorporate references to 42 U.S.C. 11408a and its more detailed instruction on transitional housing, lease and purchase procedures, and the employment or participation of homeless (or formerly homeless) individuals for the property being leased or acquired. To provide the maximum flexibility, the Agency will reserve program REO properties for no less than 30 days for sale to program eligible borrowers, as well as for sale or lease to a public agency or nonprofit organization for transitional and turnkey housing purposes. Upon receipt of written notification from a public agency or nonprofit organization seeking to purchase or lease REO property, the Agency shall withdraw the property from the market for not more than 30 days for the purpose of negotiations. If negotiations are unsuccessful, the REO

property will be relisted and sold in the best interest of the Government.

The expected result of this rulemaking is to allow the maximum use of the REO properties and foster collaboration in working to address a national shortage of transitional housing, and to provide more flexibility and increased efficiency of REO property management.

Statutory Authority

Section 510(k) of Title V the Housing Act of 1949 (42 U.S.C. 1480(k)), as amended, authorizes the Secretary of Agriculture to promulgate rules and regulations as deemed necessary to carry out the purpose of that title.

Executive Order 12866

The Office of Management and Budget (OMB) has designated this rule as not significant under Executive Order 12866.

Executive Order 12988, Civil Justice Reform

This rule has been reviewed under Executive Order 12988, Civil Justice Reform. Except where specified, all State and local laws and regulations that are in direct conflict with this rule will be preempted. Federal funds

carry Federal requirements. No person is required to apply for funding under this program, but if they do apply and are selected for funding, they must comply with the requirements applicable to the Federal program funds. This rule is not retroactive. It will not affect agreements entered into prior to the effective date of the rule. Before any judicial action may be brought regarding the provisions of this rule, the administrative appeal provisions of 7 CFR part 11 must be exhausted.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Public Law 104-4, establishes requirements for Federal agencies to assess the effect of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, the Agency 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 the Agency to identify and consider a reasonable number of regulatory alternatives

and adopt the least costly, most cost-effective, or least burdensome alternative that achieves the objectives of the rule.

This proposed 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.

Environmental Impact Statement

This document has been reviewed in accordance with 7 CFR part 1970, subpart A, "Environmental Policies." It is the determination of the Agency 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, Public Law 91-190, neither an Environmental Assessment nor an Environmental Impact Statement is required.

Executive Order 13132, Federalism

The policies contained in this rule do not have any substantial direct effect on States, on the relationship between the national government and 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.

Regulatory Flexibility Act

In compliance with the Regulatory Flexibility Act (5 U.S.C. 601 et seq.) the undersigned has determined and certified by signature of this document that this rule, while affecting small entities, will not have an adverse economic impact on small entities. This rule does not impose any significant new requirements on program recipients nor does it adversely impact proposed real estate transactions involving program recipients as the buyers.

Executive Order 12372, Intergovernmental Review of Federal Programs

This program/activity is not subject to the provisions of Executive Order 12372, which require intergovernmental consultation with State and local officials. (See the Notice related to 7 CFR part 3015, subpart V, at 48 FR 29112, June 24, 1983; 49 FR 22675, May 31, 1984; 50 FR 14088, April 10, 1985.)

Executive Order 13175, Consultation and Coordination with Indian Tribal Governments

This executive order imposes requirements in the development of regulatory policies that have tribal implications or preempt tribal laws. RHS has determined that the proposed rule does not have a substantial direct effect on one or more Indian tribe(s) or on either the relationship or the distribution of powers and responsibilities between the Federal Government and the Indian tribes. Thus, this proposed rule is not subject to the requirements of Executive Order 13175.

Programs Affected

The following programs, which are listed in the Catalog of Federal Domestic Assistance, are affected by this proposed rule: Number 10.410, Very Low to Moderate Income Housing Loans (specifically Section 502 direct loans), and Number 10.417, Very Low-Income Housing Repair Loans and Grants (specifically the Section 504 direct loans and grants).

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1995

(44 U.S.C. 3501 et seq.), the information collection activities associated with this rule are covered under OMB Number: 0575-0172. This proposed rule contains no new reporting or recordkeeping requirements that would require approval under the Paperwork Reduction Act of 1995.

E-Government Act Compliance

RHS is committed to complying with the E-Government Act, 44 U.S.C. 3601 et. seq., 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.

Non-Discrimination Policy

In accordance with Federal civil rights law and U.S. Department of Agriculture (USDA) civil rights regulations and policies, the USDA, its Agencies, offices, and employees, and institutions participating in or administering USDA programs are prohibited from discriminating based on race, color, national origin, religion, sex, gender identity (including gender expression), sexual orientation, disability, age, marital status, family/parental status, income derived from a public assistance program, political beliefs, or reprisal

or retaliation for prior civil rights activity, in any program or activity conducted or funded by USDA (not all bases apply to all programs). Remedies and complaint filing deadlines vary by program or incident.

Persons with disabilities who require alternative means of communication for program information (e.g., Braille, large print, audiotape, American Sign Language, etc.) should contact the responsible Agency or USDA's TARGET Center at (202) 720-2600 (voice and TTY) or contact USDA through the Federal Relay Service at (800) 877-8339. Additionally, program information may be made available in languages other than English.

To file a program discrimination complaint, complete the USDA Program Discrimination Complaint Form, AD-3027, found online at http://www.ascr.usda.gov/complaint_filing_cust.html and at any USDA office or write a letter addressed to USDA and provide in the letter all of the information requested in the form. To request a copy of the complaint form, call (866) 632-9992. Submit your completed form or letter to USDA by:

(1) Mail: U.S. Department of Agriculture Office of the Assistant Secretary for Civil Rights

1400 Independence Avenue, SW.,

Washington, D.C. 20250-9410;

(2) Fax: (202) 690-7442; or

(3) Email: program.intake@usda.gov.

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List of Subjects in 7 CFR Part 3550

Administrative practice and procedure, Environmental impact statements, Fair housing, Grant programs-housing and community development, Housing, Loan programs-housing and community development, Low and moderate-income housing, Manufactured homes, Reporting and recordkeeping requirements, Rural areas.

For the reasons stated in the preamble, 7 CFR part 3550 is proposed to be 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 A – General

2. Section 3550.10 is amended by:

- a. Revising the definition of *Modest housing*;
- b. Removing the definition of *National average loan*

limit;

- c. Revising the definition of *PITI ratio*;
- d. Adding definition *Principal residence* in alphabetical order; and
- e. Removing the definition of *Veterans preference* and adding the definition *Veterans' preference* in its place.

The revisions and additions read as follows:

§ 3550.10 Definitions.

* * * * *

Modest housing. A property that is considered modest for the area, has a market value that does not exceed the applicable maximum loan limit as established by RHS in accordance with § 3550.63, and not designed for income producing activities. Existing properties with in-ground pools may be considered modest; however, in-ground pools with new construction or with properties which are purchased new are prohibited.

* * * * *

PITI ratio. The amount paid by the borrower for principal, interest, taxes, insurance, and other recurring, housing related costs such as mandatory homeowner's association (HOA) dues, land lease payments (i.e. community land trusts), or other housing related assessments which

may vary by state, divided by repayment income.

* * * * *

Principal residence. The home domicile physically occupied by the owner on a permanent basis (i.e. lives there for the majority of the year and is the address of record for such activities as Federal income tax reporting, voter registration, occupational licensing, etc.).

* * * * *

Veterans' preference. A preference extended to a veteran applying for a loan or grant under this part, or the families of deceased servicemen, who meet the criteria in 42 U.S.C. 1477.

* * * * *

3. In § 3550.11, revise paragraphs (a) and (b) to read as follows:

§ 3550.11 State Director assessment of homeownership education.

(a) State Directors will assess the availability of certified homeownership education in their respective states on an as-needed basis but at a minimum every three years and maintain an updated listing of providers and their reasonable costs.

(b) The order of preference for homeownership education formats will be determined by the Agency based on

factors such as industry practice and availability.

* * * * *

Subpart B - Section 502 Origination

4. In § 3550.52, revise paragraphs (a) and (d)(6) to read as follows:

§ 3550.52 Loan Purposes.

* * * * *

(a) *Purchases from existing RHS borrowers.* To purchase a property currently financed by an RHS loan, the new borrower will assume the existing RHS indebtedness or receive new loan funds as determined by the Agency. The Agency will periodically determine whether assumptions or new loans are appropriate on a program wide basis based on the best interest of the government, taking into account factors such as funding availability and staff resources. Regardless of the method, loan funds may be used for eligible costs as defined in paragraph(d) of this section or to permit a remaining borrower to purchase the equity of a departing co-borrower.

* * * * *

(d) * * *

(6) Packaging fees resulting from the certified loan application packaging process outlined in § 3550.75. The Agency will determine the limit, based on factors such as

the level of service provided and the prevailing cost to provide the service, and such cap will not exceed two percent of the national average area loan limit. Nominal packaging fees not resulting from the certified loan application process are an eligible cost provided the fee does not exceed a limit determined by the Agency based on the level and cost of service factors, but no greater than one percent of the national average area loan limit; the loan application packager is a nonprofit, tax exempt partner that received an exception to all or part of the requirements outlined in § 3550.75 from the applicable Rural Development State Director; and the packager gathers and submits the information needed for the Agency to determine if the applicant is eligible along with a fully completed and signed uniform residential loan application.

* * * * *

5. In § 3550.53, revise paragraphs (c), (g), and (i) to read as follows:

§ 3550.53 Eligibility requirements.

* * * * *

(c) *Principal residence.* Applicants must agree to and have the ability to occupy the dwelling in accordance with the definition found in § 3550.10. If the dwelling is being constructed or renovated, an adult member of the

household must be available to make inspections and authorize progress payments as the dwelling is constructed.

* * * * *

(g) *Repayment ability.* Repayment ability means applicants must demonstrate adequate and dependably available income. The determination of income dependability will include consideration of the applicant's history of annual income.

(1) An applicant is considered to have repayment ability when the monthly amount required for payment of principal, interest, taxes, insurance, homeowner's association (HOA) dues and other recurring, housing related assessments (PITI) does not exceed thirty-five percent of the applicant's repayment income (PITI ratio). In addition, the monthly amount required to pay PITI plus recurring monthly debts must not exceed forty-three percent of the applicant's repayment income (total debt ratio).

(2) If the applicant's PITI ratio and total debt ratio exceed the percentages specified by the Agency by a minimal amount, compensating factors may be considered. Examples of compensating factors include: payment history (if applicant has historically paid a greater share of income for housing with the same income and debt level), savings history, job prospects, and adjustments for

nontaxable income.

(3) If an applicant does not meet the repayment ability requirements in this paragraph (g), the applicant can have another party join the application as a cosigner, have other household members join the application, or both.

* * * * *

(i) *Homeownership education.* Applicants who are first-time homebuyers must agree to provide documentation, in the form of a completion certificate or letter from the provider, that a homeownership education course from a certified provider under § 3550.11 has been successfully completed as defined by the provider. Requests for exceptions to the homeownership education requirement in this paragraph (i) will be reviewed and granted on an individual case-by-case basis. The State Director may grant an exception to the homeownership education requirement for individuals in geographic areas within the State where the State Director verifies that certified homeownership education is not reasonably available in the local area in any of the formats listed in § 3550.11(b). Whether such homeownership education is reasonably available will be determined based on factors including, but not limited to: Distance, travel time, geographic obstacles, and cost. On a case-by-case basis, the State

Director also may grant an exception, provided the applicant borrower documents a special need, such as a disability, that would unduly impede completing a homeownership course in a reasonably available format.

6. In § 3550.55, revise paragraphs (c) introductory text and (c) (4) and (5) to read as follows:

§ 3550.55 Applications.

* * * * *

(c) Selection for processing and funding.

Applications will be selected for processing using the priorities specified in this paragraph (c). Within priority categories, applications will be processed in the order that the completed applications are received. In the case of applications with equivalent priority status that are received on the same day, preference will first be extended to applicants qualifying for a veterans' preference. When funds are limited and eligible applicants will be placed on the waiting list, the priorities specified in this paragraph (c) will be used to determine the selection of applications for available funds.

* * * * *

(4) Fourth priority will be given to applicants seeking loans for the construction of dwellings in an RHS-

approved Mutual Self-Help project, loan application packages funneled through an Agency-approved intermediary under the certified loan application packaging process, and loans that will leverage funding or financing from other sources at a level published in the program handbook.

(5) Applications from applicants who do not qualify for priority consideration in paragraph (1), (2), (3), or (4) of this section will be selected for processing after all applications with priority status have been processed.

* * * * *

§ 3550.56 [Amended]

7. In § 3550.56:

a. Add the word "and" at the end of paragraph (b) (1);

b. Remove "; and" and add a period in its place in paragraph (b) (2); and

c. Remove paragraph (b) (3).

8. In § 3550.57, revise paragraph (a) introductory text to read as follows:

§ 3550.57 Dwelling requirements.

(a) *Modest dwelling.* The property must be one that is considered modest for the area, must not be designed for income producing purposes, or have a market value in excess of the applicable maximum loan limit, in accordance with § 3550.63, unless RHS authorizes an exception under this

paragraph (a). Existing properties with in-ground pools may be considered modest; however, in-ground pools with new construction or with properties which are purchased new are prohibited. An exception may be granted on a case-by-case basis to accommodate the specific needs of an applicant, such as to serve exceptionally large households or to provide reasonable accommodation for a household member with a disability. Any additional loan amount approved must not exceed the amount required to address the specific need.

* * * * *

9. In § 3550.59, revise paragraph (a) (2) to read as follows:

§ 3550.59 Security requirements.

* * * * *

(a) * * *

(2) No liens prior to the RHS mortgage exist at the time of closing and no junior liens are likely to be taken immediately after or at the time of closing, unless the other liens are taken as part of a leveraging strategy or the RHS loan is essential for repairs. Any lien senior to the RHS lien must secure an affordable non-RHS loan. Liens junior to the RHS lien may be allowed at loan closing if the junior lien will not interfere with the purpose or

repayment of the RHS loan. When the junior lien involves a grant or a forgivable affordable housing product, the total debt may exceed the market value provided:

(i) The RHS loan is fully secured (with allowable exceptions for the tax service fee, appraisal fee, homebuyer education and initial escrow for taxes and insurance);

(ii) The junior lien is for an authorized loan purpose identified in § 3550.52; and

(iii) The grant or forgivable affordable housing product comes from a recognized grant source such as a Community Development Block Grant or a HOME Investment Partnerships Program (HOME).

* * * * *

10. In § 3550.67, revise paragraph (c) to read as follows:

§ 3550.67 Repayment period.

* * * * *

(c) Ten years for loans not exceeding an amount determined by the Agency based on factors such as the performance of unsecured loans in the Agency's portfolio and the Agency's budgetary needs, but not to exceed ten percent of the national average area loan limit.

* * * * *

Subpart C - Section 504 Origination and Section 306C Water and Waste Disposal Grants

11. In § 3550.103, revise paragraph (e) to read as follows:

§ 3550.103 Eligibility requirements.

* * * * *

(e) *Need and use of personal resources.* Applicants must be unable to obtain financial assistance at reasonable terms and conditions from non-RHS credit or grant sources and lack the personal resources to meet their needs. Elderly families must use any net family assets in excess of \$20,000 to reduce their section 504 request. Non-elderly families must use any net family assets in excess of \$15,000 to reduce their section 504 request. Applicants may contribute assets in excess of the aforementioned amounts to further reduce their request for assistance. The definition of assets for the purpose of this paragraph (e) is net family assets as described in § 3550.54, less the value of the dwelling and a minimum adequate site.

* * * * *

12. In § 3550.104, revise paragraph (c) to read as follows:

§ 3550.104 Applications.

* * * * *

(c) *Processing priorities.* When funding is not sufficient to serve all eligible applicants, applications for assistance to remove health and safety hazards will receive priority for funding. In the case of applications with equivalent priority status that are received on the same day, preference will be extended to applicants qualifying for a veterans' preference. After selection for processing, requests for assistance are funded on a first-come, first-served basis.

13. In § 3550.106, revise paragraph (a) to read as follows:

§ 3550.106 Dwelling requirements.

(a) *Modest dwelling.* The property must be one that is considered modest for the area, must not be designed for income producing purposes, or have a market value in excess of the applicable maximum loan limit, in accordance with §3550.63.

* * * * *

14. In § 3550.108, revise paragraph (b) (1) to read as follows:

§ 3550.108 Security requirements (loans only).

* * * * *

(b) * * *

(1) Loans where the total section 504 indebtedness does not exceed an amount determined by the Agency based on factors such as average costs for title insurance and closing agents compared to average housing repair costs, but no greater than twenty percent of the national average area loan limit.

* * * * *

15. In § 3550.112, revise paragraphs (a) introductory text, (a) (1), and (c) to read as follows:

§ 3550.112 Maximum loan and grant.

(a) *Maximum loan permitted.* The sum of all outstanding section 504 loans to one household for one dwelling may not exceed an amount determined by the Agency based on factors such as average loan amounts and repair costs, but no greater than twenty percent of the national average area loan limit.

(1) Transferees who have assumed a section 504 loan and wish to obtain a subsequent section 504 loan are limited to the difference between the unpaid principal balance of the debt assumed and the maximum loan permitted.

* * * * *

(c) *Maximum grant.* The lifetime total of the grant assistance to any one household for one dwelling may not exceed an amount established by the Agency based factors

such as average lifetime grant amounts and repair costs, but no greater than five percent of the national average area loan limit. No grant can be awarded when the household has repayment ability for a loan.

16. In § 3550.113, revise paragraph (b) to read as follows:

§ 3550.113 Rates and terms (loans only).

* * * * *

(b) *Loan term.* The repayment period for all section 504 loans will be 20 years.

Subpart D - Regular Servicing

17. In § 3550.162, revise paragraphs (b) (1) introductory text and (b) (1) (ii) to read as follows:

§ 3550.162 Recapture.

* * * * *

(b) * * *

(1) *General.* The amount to be recaptured is determined by a calculation specified in the borrower's subsidy repayment agreement and is based on the borrower's equity in the property at the time of loan pay off. If there is no equity based on the recapture calculation, the amount of principal reduction attributed to subsidy is not collected. The recapture calculation includes the amount of

principal reduction attributed to subsidy plus the lesser of:

* * * * *

(ii) A portion of the value appreciation of the property subject to recapture. In order for the 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.

* * * * *

Subpart E - Special Servicing

18. In § 3550.207, revise paragraphs (b) (2) and (c) and remove paragraph (d) to read as follows:

§ 3550.207 Payment moratorium.

* * * * *

(b) * * *

(2) At least 30 days before the moratorium is scheduled to expire, the borrower must provide financial information needed to process the re-amortization of the loan(s).

(c) *Resumption of scheduled payments.* When the moratorium expires or is cancelled, the loan will be re-amortized to include the amount deferred during the

moratorium and the borrower will be required to escrow. If the new monthly payment, after consideration of the maximum amount of payment subsidy available to the borrower, exceeds the borrower's repayment ability, all or part of the interest that has accrued during the moratorium may be forgiven so that the new monthly payment optimizes both affordability to the borrower as well as the best interest of the Government.

Subpart F - Post-Servicing Actions

19. In § 3550.251:

- a. Revise paragraphs (c) (4) and (5);
- b. Remove paragraph (C) (6);
- c. Revise paragraph (d) (2);
- d. Remove paragraph (d) (3);
- e. Redesignate paragraph (d) (4) as (d) (3).

The revisions read as follows:

§ 3550.251 Property management and disposition.

* * * * *

(c) * * *

(4) *Sale of program REO properties.* For no less than 30 days after a program REO property is listed for sale, the property will be reserved for sale to eligible direct or guaranteed single family housing very-low, low- or moderate income applicants under this part or part 3555 of

this title, and for sale or lease to nonprofit organizations or public bodies providing transitional housing and turnkey housing for tenants of such transitional housing in accordance with 42 U.S.C. 11408a. Offers from eligible direct or guaranteed single family housing applicants are evaluated at the listed price, not the offering price. Priority of offers received the same day from eligible direct or guaranteed single family housing applicants will be given to applicants qualifying for veterans' preference, cash offers from highest to lowest, then credit offers from highest to lowest. Acceptable offers of equal priority received on the same business day are selected by lot. After the expiration of a reservation period, REO properties can be bought by any buyer.

(5) *Sale by sealed bid or auction.* RHS may authorize the sale of an REO property by sealed bid or public auction when it is in the best interest of the Government.

(d) * * *

(2) RHS shall follow the standards and procedures in 42 U.S.C. 11408a for the sale or lease of an REO property to a public agency or nonprofit organization. The terms of the sale and lease, and the entity seeking to purchase or

lease the REO property, must meet the requirements in 42
U.S.C. 11408a.

* * * * *

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