

U. S. Department of Housing and Urban Development
Washington, D.C. 20410-8000

DEC 31 2001

OFFICE OF THE ASSISTANT SECRETARY
FOR HOUSING-FEDERAL HOUSING COMMISSIONER

MORTGAGEE LETTER 2001-30

TO: ALL APPROVED MORTGAGEES
ALL APPROVED NONPROFIT ORGANIZATIONS
ALL PARTICIPATING GOVERNMENT ENTITIES

SUBJECT: Nonprofit Organization and Government Entity Participation in Single Family FHA Activities: Clarification of Net Development Cost Calculation; Expansion of the Use of the Net Development Cost Calculation and Land Use Restriction Addendum to Properties Sold at a Discount of 10 percent or more; Program Definitions; and List of Relevant Documents

This Mortgagee Letter clarifies the calculation of Net Development Cost and expands the use of the Net Development Cost calculation to HUD properties sold at a discount of 10 percent or more. It applies to government entities and qualified nonprofit organizations that have been pre-approved by HUD to purchase HUD Homes (also referred to as Real Estate Owned, or REO properties in other Mortgagee Letters). Nonprofit organizations and government entities must pass on the discount received from HUD to increase homeownership opportunities for low- and moderate-income families and individuals. Appendix A to this Mortgagee Letter provides a detailed list of the costs allowed in the Net Development Cost calculation.

This Mortgagee Letter also expands the use of the Land Use Restriction Addendum to all HUD homes sold to nonprofit organizations and government entities at a discount of 10 percent or greater, effective for all sale contracts executed on or after one month from the date of this Mortgagee Letter. The addendum, to be attached to all Sales Contracts for these discounted properties, stipulates that the property be utilized to expand affordable housing opportunities as stated in 24 CFR 291.301(3). The Land Use Restriction Addendum is set forth in Appendix B to this Mortgagee Letter. Discounted homes purchased through the Dollar Homes, Asset Control Area (ACA), and Officer/Teacher Next Door programs continue to be exempt from these restrictions.

Appendix C to this Mortgagee Letter is a list of definitions for terms commonly used by lenders, nonprofit organizations, and government entities in FHA Single Family Housing

programs and Appendix D to this Mortgagee Letter is a summary reference guide of HUD Handbooks, Mortgagee Letters, and Housing Notices that apply to nonprofit participation in Single Family Housing activities.

Questions regarding this Mortgagee Letter should be directed to the FHA Homeownership Centers in Atlanta (1-888-696-4687), Denver (1-800-543-9378), Philadelphia (1-800-440-8647) or Santa Ana (1-888-827-5605).

Sincerely,

John C. Weicher
Assistant Secretary for Housing-
Federal Housing Commissioner

Attachments

Net Development Cost

The Net Development Cost is composed of the allowable property acquisition costs plus allowable rehabilitation, holding, and selling costs nonprofit organizations or government entities incur when purchasing HUD Homes at discounted prices, redeveloping the properties for resale, and selling those properties. The Net Development Cost calculation applies to all HUD Homes sold to nonprofit organizations and government entities at a 10 percent or greater discount regardless of the financing instrument (FHA, conventional mortgage, or cash), except for HUD Homes purchased through the Dollar Homes, ACA, and Officer/Teacher Next Door programs.

The purpose of these discounts and the limits on development costs is to make housing affordable to low-to-moderate income families. The Department limits the costs that are eligible to be included in the Net Development Cost calculation and prohibits the nonprofit organization or government entity from reselling the repaired or improved properties at prices in excess of 110 percent of the net development cost calculation. If the nonprofit organization's or government entity's re-sale price of the HUD Home exceeds 110 percent of the net development cost, or if non-allowable items that are included in net development cost result in an excessive sales price, the HUD-approved nonprofit organization or government entity must use the excess profit to pay down the existing mortgage associated with that particular re-sale.

Costs Allowed in Calculating the Net Development Cost

Only the costs specifically included in the following list, within the prescribed limitations and/or conditions, may be included in calculating the Net Development Cost.

1. Discounted purchase price paid to HUD
2. Upon the purchase of the property from HUD, financing and closing costs actually incurred, which must be reasonable and customary for the area in which the property is located, limited to the following:
 - a. The actual loan origination fee, not to exceed 1 percent
 - b. Supplemental loan origination fee (203(k) mortgages only)
 - c. Credit report fee
 - d. Net tax and insurance escrow deposit
 - e. Settlement fee (buyer's portion)
 - f. Discount points
 - g. Hazard insurance premiums
 - h. Lender's title insurance policy premium
 - i. Owner's title insurance policy premium
 - j. Notary fees
 - k. Recording fees
 - l. Appraisal fee
 - m. Courier fees

- n. Document preparation fees
- o. Attorney fees for services performed in connection with the loan closing, such as review of abstract or preparation of closing documents
- p. Flood plan certification and fee for determination of flood zone

3. For the time period the nonprofit organization or government entity holds title, the following costs, limited to amounts that are reasonable and customary for the area in which the property is located:

- a. Fees paid to an approved 203(k) consultant for work write-ups, cost estimates, and inspections only. See Mortgagee Letter 95-40 for allowable fees.
- b. Property management, but only if related to periodic inspection and/or minor maintenance of the property.
- c. Architectural fees, but only if the services are provided by a licensed architectural firm or individual architect.
- d. Rehabilitation costs, which are the total verifiable contractor and vendor expenditures incurred in the actual re-construction, repair, restoration and physical improvement of the property. Rehabilitation costs are limited to the actual price paid to the contractor for completing each repair or improvement, and may also include expenditures for mechanical systems inspections, sewer and well inspections, repair inspections, foundation certifications for manufactured homes obtained from a licensed engineer, and roof inspections from a licensed contractor. HUD may require canceled checks and corresponding receipts as proof of rehabilitation costs. When calculating the Net Development Cost, nonprofit organizations or government entities using grant funds for the rehabilitation of HUD Homes acquired at a discount, can not include the cost of the rehabilitation that is paid for by those grant funds.
- e. Cost of public and municipal services and/or utilities and real property taxes for the subject premises, except for delinquent interest or penalty charges incurred as a result of failure of purchaser to pay these expenses in a timely manner.
- f. Cost of termite inspection and extermination services.
- g. Homeowners Association fees or Condo Association fees.
- h. Permits and other fees paid to units of state and local governments that are required by rule, law, regulation or other legally binding mandate that must be paid before initiating or completing the rehabilitation or property improvement.
- i. Survey costs.
- j. Hazard and liability insurance premiums.
- k. Principal and Interest portion of mortgage payments (P&I) limited to a maximum of six months (P&I) mortgage payments, less any and all rents received. If the property is resold in less than 180 days, the mortgage payment credit must be prorated on the basis of the actual payments made.

4. Upon the resale of the property to a new purchaser, only the following seller closing costs that are actually incurred, limited to amounts that are reasonable and customary for the area in which the property is located:
 - a. 1/2 of closing agent-fee (sellers portion)
 - b. Electronic wiring fees
 - c. Courier and mailing fees (seller's documents only)
 - d. Title insurance premium (owners policy only)
 - e. State, county, or city tax stamps, if local law requires the seller to pay these costs
 - f. Homeowners warranty premium
 - g. Environmental hazard certification
 - h. Document preparation fee (seller's documents only)
 - i. Recording (deed only) and reconveyance fees
 - j. Sales commissions for real estate broker/agent services
 - k. Condominium transfer fee

Costs Not Allowed in Calculating the Net Development Cost

Costs not listed above are ineligible and cannot be included in the Net Development Cost calculation. Ineligible costs include, but are not limited to:

1. General administration cost of the nonprofit organization's or government entity's Affordable Housing Program and homeownership programs, including overhead and staffing costs.
2. Housing developer fees and/or real estate consultant fees.
3. Sales bonuses and sales incentives (other than sales commissions) for selling or listing real estate brokers/agents.
4. Gifts to the eventual purchasers for down payment, financing or closing costs, and any other purchaser-related expenses associated with their purchase of the property.
5. Development, maintenance and management costs related to other properties in the nonprofit organization's or government entity's inventory.
6. Delinquent property tax penalties and interest.
7. Mortgage payment late fees, pre-payment penalties, pay-off quote fees and fax charges.
8. Any development costs that are paid from local, state, or Federal grant funds (such as, but not limited to HOME or CDBG funds) that would otherwise be allowable in the NDC calculation.

This list of definitions applies to terminology only as applied to FHA's Single Family Housing Nonprofit Programs.

203(b) - An FHA mortgage insured under Section 203(b) of the National Housing Act for the acquisition of a 1-4 unit property by an owner occupant buyer, a qualified nonprofit organization that has been pre-approved to participate by HUD, or a participating government entity.

203(k) - An FHA mortgage insured under Section 203(k) of the National Housing Act. This mortgage is for the acquisition and rehabilitation of a 1-4 unit property by an owner occupant buyer, a qualified nonprofit organization that has been pre-approved to participate by HUD, or a participating government entity.

203(k) Consultant - A technical expert, selected by the mortgagee from FHA's roster of qualified 203(k) consultants to assist mortgagors for a fee with the preparation of the rehabilitation plan for a property being financed with HUD's 203(k) Rehabilitation Insured Mortgage. A 203(k) Consultant may also perform draw inspections. The mortgagor, and not HUD or the mortgagee, is responsible for paying the fees charged by the 203(k) consultant. See Mortgagee Letter 94-11 for a description of the 203(k) Consultant's role. See Mortgagee Letter 95-40 for the maximum allowable fees that a 203(k) Consultant can charge. See Mortgagee Letter 00-25 for a description of how individuals can apply for placement on FHA's roster of qualified 203(k) consultants.

Affordable Housing Program - A program, as described in a written proposal submitted to HUD, operated by a nonprofit in specific geographical areas in which the nonprofit provides affordable homeownership opportunities for low-to-moderate income buyers by purchasing, rehabilitating, and reselling HUD Homes to these buyers. The program can include other homeownership activities, such as counseling. See Mortgagee Letter 2002-01, Attachment 2, for a description of the items that a nonprofit should address in the written proposal that describes its program.

Allowable Net Development Cost - Costs that are permitted to be included in the Net Development Cost calculation.

Conflict of Interest - An inappropriate relationship that compromises the private interests and official responsibilities of a person in a position of trust. It is a conflict of interest for a nonprofit to employ staff who also work for and receive financial benefits from a for-profit entity that is providing the nonprofit with services related to the nonprofit's affordable housing plan. Board members must serve on a voluntary basis, and may not be paid nor receive any compensation for any services they provide in the implementation of the nonprofit's affordable housing program.

FHA will collect information on the job responsibilities of all Board members to ensure that their occupational activities and obligations do not conflict with the work of the nonprofit. HUD strictly prohibits the sale or lease of properties with FHA financing and/or discounted HUD Homes to any of the nonprofit's officers, directors, elected or appointed officials, employees, or business associates, either during their tenure or for one year thereafter, or to any individual who is related by blood, marriage, or law to any of the above.

Consultant - A real estate, financial or management professional who assists a nonprofit organization with housing development activities. Consultant fees, except for certain fees by 203(k) Consultants, are not allowable net development costs.

Direct Sales Program - A program under which qualified nonprofit organizations that have been pre-approved to participate by HUD, and government entities can purchase properties at a discount. The participation of a HUD registered real estate broker is not required.

Gift Funds - A monetary gift to a homebuyer that does not require repayment and is given for downpayment or closing costs. The following individuals and groups are acceptable sources of gift funds: a relative of the homebuyer, the homebuyer's employer or labor union, a charitable organization, a government agency or public entity that has a program to provide homeownership assistance to low- and moderate- income persons or first time homebuyers, or a close friend with a clearly defined interest in the homebuyer. Gifts to a homebuyer are not Allowable Net Development Costs. See paragraph 2-10.C, Handbook 4155.1, REV-4, CHG-1, "Mortgage Credit Analysis for Mortgage Insurance on One to Four Family Properties", and Mortgagee Letter 97-5.

Homeownership Center (HOC) - Any one of the four HOCS, which are located in Atlanta, GA; Denver, CO; Philadelphia, PA; and Santa Ana, CA. The jurisdiction of each HOC can be found online at: <http://www.hud.gov/offices/hsg/sfli/hoc/hsghocs.cfm>.

Housing Developer - An individual or entity that performs activities such as property acquisition, inspection, construction, rehabilitation, financing, marketing or sales. Housing Developer fees are not allowable Net Development Costs.

Income Verification - The act of obtaining documentation that establishes that the resale buyers' income was at or below the defined percent of the area median income when adjusted for family size. Such documentation may include a copy of the buyer's IRS W-2 form, pay stubs, employer verification, mortgage credit analysis worksheet, loan application, or tax returns. See Mortgagee Letter 2002-01, Attachment 4, for the requirement to retain income verification.

Land Use Restriction Addendum - A legally binding contractual agreement between the Department of Housing and Urban Development and the nonprofit organization or government entity imposing restrictions on the resale of a HUD home that the nonprofit organization or government entity purchased at a discount of 10 percent or greater. See Appendix B.

Low to Moderate Income Buyer - A purchaser whose income does not exceed the defined percent of the median income, when adjusted for family size, for the area in which the property is located.

Non-Allowable Net Development Costs - Those costs that are not permitted to be included in the Net Development Cost calculation.

Property Manager - Maintains a property that is in the inventory of a nonprofit organization or government entity. Typical activities of a property manager are lawn care, trash removal, building security, and repairs of minor damage caused by vandalism or the weather. Property management fees related to the periodic inspection and/or minor maintenance of a property are allowable Net Development Costs to the extent that they are reasonable and customary for the area in which the property is located. See Mortgagee Letter 97-5 and Appendix A.

Reasonable and Customary Fees - Those fees that are consistent with recent historical fees for the area in which the real estate transaction occurs. Fees included in the Net Development Cost calculation must be reasonable and customary, and HUD will disallow excessive fees.

Revitalization Area - An area designated by HUD that meets the criteria stated in Housing Notice H 00-16.

Secondary Financing Program - Financing in the form of second mortgages that may be forgivable, run for a specific term, with or without monthly mortgage payments. Subject to certain conditions, this financing may be used for a borrower's downpayment, closing costs, prepaid expenses, or any combination of these. See paragraph 1-13, Handbook 4155.1, Rev-4, CHG-1, "Mortgage Credit Analysis for Mortgage Insurance on One-to-Four Family Properties" and Mortgagee Letters 94-2 and 00-08.

Appendix D

List of Reference Documents

The following list of documents applies to qualified nonprofit organizations that have been pre-approved to participate in HUD's Single Family Housing Programs. Nonprofit organizations must have knowledge of, and comply with, the instructions contained in these documents, any amendments to these documents, and any future documents issued.

HUD periodically publishes new documents relating to the activities of non-profit organizations and government entities. Non-profit organizations and government entities can register for automatic e-mail notification of new HUD handbooks, mortgagee letters and housing notices on the Internet at: <http://www.hud.gov/offices/hsg/sfh/ref/hsszrcont.cfm>

All of the documents listed herein may be accessed online at:
<http://www.hudclips.org/cgi/index.cgi>

HUD Regulations

24 CFR Part 291, governs the sales of HUD homes

24 CFR Part 203, governs HUD's Single Family Mortgage Insurance programs

HUD Mortgagee Letters

ML# 92-33 Clarifications and Modifications to the 203(k) Program

ML# 94-02 Secondary financing for Nonprofit Agencies

ML# 94-11 Revisions to the 203 (k) Program

ML# 95-40 Revisions to the 203(k) Mortgage Program

ML# 96-21 203(k) w/Participation by State & Local Housing Agencies
and Non-Profit Organizations

ML# 96-52 Non Profit Agencies as Mortgagors

ML# 96-59 Moratorium on Investor Loans in Conjunction with the 203(k)

ML# 97-05 Revised Escrow Commitment Procedure

ML# 98-02 Combining EEM and 203(k)

ML# 98-11 Concerns about 203 (k) Underwriting, Loan Processing

ML# 00-08 Nonprofit Agency Participation in Single Family FHA Activities

ML# 00-25 203(k) Mortgage Program - Single Family Loan Production

ML 2002-01 Nonprofit Participation in FHA Single Family Activities - New Requirements and
Restrictions

HUD Handbooks

HUD Handbook 4155.1 Chapter 1: Underwriting the mortgage, Section 1-5 Non profit
organizations and state and local government agencies

HUD Handbook 4240.4 REV-2: 203(k) Rehabilitation Home Mortgage Insurance

HUD Notices

HUD Property Disposition Notice 94-74

HUD Property Disposition Notice 00-16

HOC National Reference Guide

Secondary financing by non profit agencies Chapter 2 page 2-5