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Veterans Benefits Administration
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FOREWORD

a. This publication is a guide for program participants who hold and/or service VA-guaranteed home loans. It contains the servicing, claims, and conveyance policies and procedures applicable to VA loans, as well as a copy of the part of the Code of Federal Regulations dealing with VA loans.

b. The issuance of a VA guaranty on a loan is in part predicated upon the understanding that adequate loan servicing will be performed by the holder. This requirement is implied in the law and expressed in the regulations. Failure to comply with VA regulations regarding servicing, claims, and conveyance may result in a reduction of the amount of claim payable by VA. A pattern of failure may result in suspension from program participation.

c. Lending institutions and servicers are generally anxious to avoid a foreclosure and strive to maintain a low delinquency record. While many loan holders designate an agent to collect loan installments and/or perform other functions to protect the interests of the holder, it is the holder that remains responsible for compliance with the law and regulations governing VA-guaranteed loans.

d. The procedures and policies outlined in this handbook are intended to guide holders and servicers in servicing loans under the provisions of chapter 37, title 38, United States Code. Nothing contained in this handbook should be construed as modifying or otherwise altering any of the regulations affecting the Loan Guaranty Program in part 36 of title 38, Code of Federal Regulations or in title 38 of the United States Code. If there appears to be a discrepancy between the procedures and policies in this handbook and the related regulations or governing law, the latter will govern. Where possible, the number of the regulation related to VA policies and procedures is given in parenthesis.

VA Regional Office Structure

a. The Veterans Benefits Administration operates a network of 58 decentralized field offices. Forty-six of these offices have Loan Guaranty operations. See appendix A for a list of VAROs (VA Regional Offices). Any correspondence regarding a specific loan, including the required notices of default and intention to foreclose, should be sent to the VARO with a Loan Guaranty operation that has jurisdiction over the county where the property securing the loan is located.

b. VA attempts to uniformly implement its major policies and procedures. However, regional offices are given some discretion in structuring their operations, which may result in variances on certain policies and procedures between regional offices. In addition, State laws regarding mortgages and foreclosures vary considerably. This also results in differences between VAROs, especially regarding the type of documents required and steps to be taken in foreclosure, in conveying title to acquired property to VA, and in pursuing alternatives to foreclosure. Each VARO issues Loan Guaranty Bulletins on the policies or procedures that may be different in their jurisdiction. Holders should be on the

mailing list of each VARO that has jurisdiction over an area where they hold loans. VA expects holders to be aware of the requirements of each local office .

Definitions (38 CFR 36.4301)

a. An **automatic lender** is one that may process a loan or assumption without submitting the credit package to VA for review, pursuant to 38 U.S.C. 3702(d)

b. A **credit package** consists of any information, reports, or verifications used by a lender, holder, or authorized servicing agent to determine the creditworthiness of an applicant for a VA-guaranteed loan or the assumer of such a loan. This includes the prospective purchaser's application.

c. A **holder** is any institution that owns a loan guaranteed by VA. The holder is ultimately responsible for ensuring that all applicable VA policies, procedures, and regulations are followed. In this handbook, the word "holder" refers to both the actual loan holder and any designated servicing agent. When loans have been pooled through the GNMA (Government National Mortgage Association), whoever services the loan and has the right to file and receive payment of a claim under guaranty is considered the holder.

d. A **servicing agent** is an agent designated by the loan holder to collect installments on the loan and/or perform other functions to protect the interests of the holder. The servicing agent may perform any of the actions discussed in this handbook on behalf of the holder, including loan assumptions if the servicing agent is also an automatic lender.

e. A **default** is any failure of a borrower to comply with the terms of a loan agreement. If a payment due on the first of the month has not been received on the second, VA considers the loan to be in default on the second. If the payment has still not been received 30 days later, VA considers the loan to have been in default for 30 days.

f. The VA LIN (**VA Loan Identification Number**) is a 12 position unique identifier for each loan guaranteed by VA. The VA LIN consists of a two-position numeric code for the regional office which has jurisdiction over the loan (OJ), a two-position numeric code for the regional office which originated the loan (OO), a one-position code for the type of loan, and a seven position serial number or loan number. Appendix B, Circular 26-93-14, VA Loan Identification Numbers, provides a description of the VA LIN.

R. J. Vogel
Under Secretary for Benefits

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CHAPTER 1. CURRENT SERVICING

1.01 General

Holders are expected to service VA loans in conformity with procedures customarily used by prudent lenders in servicing portfolios of similar conventional loans. Loan holders' performance is also measured by their compliance with applicable Federal statutes, such as the RESPA (Real Estate Settlement Procedures Act), as amended, and laws and regulations governing the VA loan program.

1.02 Accounting Records (38 CFR 36.4330)

A record must be maintained of loan payments received and disbursements made and the dates of all transactions for each account. Since these records must accompany any claim filed under the guaranty, holders are encouraged to obtain and retain them for loans acquired through purchase or servicing transfers. If a claim is filed without complete accounting records, VA will assume that all payments were received and applied as scheduled during the period for which no records are provided.

1.03 Servicing Organization

a. **Servicing Operations** (38 CFR 36.4346(b))

(1) Loan holders are allowed wide latitude in organizing their servicing operations, but there are some VA requirements. All borrowers must be informed of the procedures and systems available for obtaining answers to inquiries. Holders will be reminded of these systems at least annually.

(2) Holders must either:

(a) Locate their servicing operations within a 200 mile radius of their loan accounts; or,

(b) Provide toll-free or collect calling services at an office capable of responding to requests for information.

b. **Quality Control Procedures.** (38 CFR 36.4346(l)) Loan holders must have internal controls which periodically assess the quality of servicing of VA loans and to assure that VA's servicing standards are met. An internal assessment of the holder's servicing activity must be conducted at least annually. The holder should:

(1) Collect and maintain appropriate data on delinquency and foreclosure rates to enable it to evaluate the effectiveness of its collection efforts;

(2) Determine how its VA delinquency and foreclosure rates compare with rates in reports published by the industry, investors and others; and,

(3) Analyze significant variances between its foreclosure and delinquency rates and those found in reports and publications and take appropriate corrective action.

This data and analysis must be provided to VA upon request. Requests may be made by VA's Central Office, lender/servicer monitoring units or VAROs.

c. **Duty to Respond to Written Borrower Inquiries.** RESPA, which was amended in 1990, requires the following strict deadlines for response to written borrower inquiries.

(1) **Twenty Business Days to Acknowledge**. A qualified written request from a borrower, or agent of the borrower, relating to the servicing of his/her loan must be acknowledged in writing within 20 business days of receipt, unless the action requested is taken within 20 business days. A qualified written request must enable a servicer to identify the name and account of the borrower, and provide sufficient detail as to why the account is in error or other information requested by the borrower.

(2) **Sixty Business Days to Resolve**. Within 60 business days of receipt of a qualified written request (as defined in subpar. (1) above) from a borrower or agent of the borrower about to the servicing of his/her loan, the servicer must complete an investigation and notify the homeowner of its results. The findings from this investigation should be used to determine which of the following three courses of action should be taken: correct the borrower's account and notify the borrower in writing of the correction; provide written explanation to the borrower if the account is correct; or, write the borrower with an explanation if the requested information is unavailable. The name and telephone number of the servicer to contact must be provided to the borrower in the notification.

(3) **Prohibition Against Reporting to Credit Agencies**. During the 60 day investigation period (as defined in subpar. (2) above), information indicating a late mortgage payment on the account under investigation may not be reported to credit agencies.

1.04 Statement for Income Tax Purposes (38 CFR 36.4346(c))

VA requires that within 60 days after the end of each calendar year, the holder must furnish to the borrower a statement of the interest paid and the taxes disbursed from the escrow account during the preceding year. Since RESPA requires that this statement be furnished within 30 days after the end of the calendar year, holders must satisfy the RESPA requirement. At the borrower's request, the holder must furnish a statement of the escrow account that will enable the borrower to reconcile the account.

1.05 Advances (38 CFR 36.4313)

a. A holder may advance any amount reasonably necessary and proper for:

(1) Maintenance or repair of the security;

(2) Payment of accrued taxes, special assessments, ground or water rents;

(3) Premiums on fire, flood, or other casualty insurance against loss or damage to the property; and,

(4) If the commitment for the loan was made on or after March 1, 1988, one-half of one percent of the funding fee due on a transfer if it is not paid at the time of transfer.

b. The advance may be added to the guaranteed indebtedness. VA does not regulate the amount of advances that are allowable on a national basis, either as charges to the borrower or for purposes of claim computation, but VA regional offices set limits on amounts they consider reasonable. See paragraph 4.17, Acceptable Expenses, for more information.

c. Advances for payment of condominium or PUD homeowners association assessments may not be included in any accounting between a holder and VA without prior approval by VA.

1.06 Extensions and Reamortizations (38 CFR 36.4314)

a. **Conditions.** A loan may be extended or reamortized provided:

(1) The loan is in default or default is imminent; and,

(2) The borrower is a reasonable credit risk, based on a review by the holder of the borrower's creditworthiness, including a current credit report; and,

(3) At least 80 percent of the loan balance extended will amortize over the remaining term of the loan (or, for loans with a term of less than 30 years, the lesser of the economic life of the security or 30 years from the date of origination); and,

(4) No obligor is released from personal liability.

Otherwise, prior approval must be obtained from VA.

b**. Terms.** Any agreement to extend or reamortize the loan must be in writing and signed by the holder and the borrower. Accrued unpaid interest may be included in the loan indebtedness extended or reamortized. A deficit in the tax and insurance account

may also be included in the indebtedness to bring the account up to the level it would have been had the borrower paid the required installments timely.

c. **Notification to VA.** Notify VA of the terms of the agreement (preferably a copy of the extension or reamortization agreement) after the agreement has been executed, along with a copy of the credit report.

1.07 Prepayments (38 CFR 36.4310)

a. **Requirements.** The borrower has the right to prepay at any time, without premium or fee, the entire indebtedness or any amount not less than the next monthly principal installment or $100, whichever is less. The holder retains the option to accept prepayment amounts which are smaller than the minimum required by regulation. Any prepayment less than payment in full which is made on a day other than an installment due date need not be credited until the following installment due date, or 30 days after the prepayment, whichever is earlier. Payment in full must be accepted and credited to the loan account when tendered, and no interest may be charged thereafter.

b. **Reapplication.** The holder and the borrower may agree at any time to re-apply prepayments to cure or prevent a default.

1.08 Servicing Fees

a. **Late Charges.** (38 CFR 36.4311(d)) A late charge may be collected on any installment received more than 15 days after its due date, provided the loan instruments contain a provision for a late charge.

(1) For example, a late charge may <u>not</u> be collected on an installment due on the first of the month if it is paid on or before the 16th of the month, but may be collected if the installment is paid on or after the 17th of the month.

(2) The late installment must be paid before the late charge is collected.

(3) The late charge may <u>not</u> be:

(a) More than 4 percent of any installment (principal, interest, and escrow for taxes and insurance);

(b) Based on an amount greater than the past due amount;

(c) Collected from the escrow account or from an escrow surplus without prior approval of the borrower;

(d) Deducted from regular payments; or,

(e) Included in a claim under the guaranty or in any accounting to VA.

(4) Late charges discourage late payments only if the borrower is able to pay on time but does not do so. If a borrower is cooperative but unable to pay, or if collection of late charges could prevent a borrower from reinstating a delinquent account, consideration should be given to waiving the late charge.

b**. Other Fees.** Fees for services outside the scope of the usual mortgage transaction depend on the terms of the loan agreement and should be determined by the parties involved. However, such charges must be reasonable, considering the work involved and the amount customarily charged in the locality. The charges listed below, while not approved by VA, are not considered improper when they are customary, agreed to by the parties, permissible under the loan agreement and are reasonable in amount:

(1) Loan assumption fees. (See pars. 1.13 and 1.14);

(2) Processing and reprocessing checks which are returned to the holder for insufficient funds;

(3) Substitution of hazard insurance policies during the life of a previously furnished policy, when substitution is made at the request of the mortgagor;

(4) Processing partial releases of the mortgaged property;

(5) Processing subordination agreements;

(6) Modification of the mortgage by a formal written extension or reamortization agreement; or,

(7) Marking the mortgage satisfied if authorized or not prohibited by local law.

1.09 Taxes and Insurance

a**. Payment of Taxes.** Security instruments uniformly require the obligor to pay taxes timely to prevent a lien with priority over the mortgage. Failure to pay taxes timely must be reported to VA if it continues for 180 days (38 CFR 36.4315(a)(2)). Most security instruments require maintenance of an escrow account by the holder to ensure payments are timely. Since VA requires the holder to maintain the priority status of the mortgage lien (38 CFR 36.4325(b)(1)), internal controls should be in place to confirm payment of taxes by the holder or the borrower.

b**. Maintenance of Hazard Insurance.** (38 CFR 36.4326) It is the holder's responsibility to assure that insurance policies are maintained in an amount sufficient to protect the security against risks or hazards and to the extent customary in the locality. Questions about the insurance coverage should be referred to the VA regional office of

jurisdiction. Subject to reasonable requirements of mortgagees, borrowers may choose their insurance carrier.

c. **Prohibitively High Premiums**

(1) Holders should not pay prohibitively high insurance premiums for force-placed coverage without prior approval of VA. If the hazard insurance is canceled (other than for nonpayment of premium) or renewal is refused, holders should attempt to obtain coverage through a State pool or otherwise. If coverage cannot be obtained except at prohibitive cost, the holder should promptly send VA the following information:

(a) The reason for cancellation or for the refusal to renew the coverage;

(b) The evidence of efforts made to obtain coverage and if obtainable, the lowest cost for such coverage;

(c) The amount and type of coverage of the policy being canceled or not renewed;

(d) The condition and current estimated value of the property improvements and the cost of any repairs required to obtain coverage;

(e) The current estimated value of the land; and,

(f) The current unpaid principal balance of the loan.

(2) Upon receipt of notification, VA will determine whether or not it is in VA's interest to give the holder assurance that a future claim under guaranty will not be adjusted for failure to maintain hazard insurance and advise the holder of the determination.

d. **Insurance During Loan Termination.** When a loan is being terminated and existing coverage has been canceled or renewal refused and the holder is unable to obtain hazard insurance except at high cost, the holder should advise VA. At the same time, the holder may request that VA not make a claim adjustment for failure to maintain hazard insurance in the event of an uninsured loss. Alternatively, the holder may choose to obtain high risk insurance rather than rely on receiving VA's assurance that a future claim would not be adjusted for failure to obtain hazard insurance. In such cases VA will partially reimburse the cost of high risk insurance in the claim. Reimbursement is based upon the portion of the premium attributable to coverage to the date of loan termination or to the date termination should have occurred (i.e., the cut-off date), whichever is earlier. The percentage of guaranty is then applied to this portion of the premium. The resulting amount is payable in the claim.

e. **Amount Required.** The amount of hazard insurance required is limited to the insurable value of the property or the current loan balance, whichever is less. The borrower may take out a larger policy if desired.

f. **Flood Insurance.** (38 CFR 36.4326) Flood insurance is required on loans closed on and after March 2, 1974, located in a special flood hazard area designated by HUD (Department of Housing and Urban Development) where flood insurance is available under the National Flood Insurance Program. The amount of insurance should be the outstanding balance of the loan or the maximum limit of coverage available, whichever is less.

g. **Application of Loss Payments** (38 CFR 36.4326)

(1) All payments for insured losses must be applied to the restoration of the security or to the loan balance. (See par. 6.06d(2).) Any other disposition must be approved in advance by VA, unless there is a balance remaining after the security has been fully restored.

(2) Settlement of a total or near total loss case should be sufficient to restore the security. When it appears that settlement proceeds will not be sufficient to pay off the loan balance or to restore the security, holders should consult VA before consenting to an insurance settlement. The holder should send VA a copy of the claim adjuster's report giving a detailed breakdown of the damage sustained. VA will also inspect the property before any loss settlement and estimate the cost of repairs.

(3) If the settlement proceeds are not to be applied to the loan balance, VA can assist holders in obtaining the services of compliance inspectors, at the holder's or borrower's expense, to assure satisfactory restoration of the security.

(4) To minimize the possibility that a claim may be adjusted for failure to obtain an adequate loss settlement, holders are encouraged to advise VA as soon as a major loss has occurred and obtain VA's estimate of the cost of restoration before accepting a loss settlement. Holders should also be cautious about completing foreclosure while a loss is pending settlement because sale proceeds may affect settlement. In some jurisdictions, it may be possible to have a disputed settlement adjudicated as part of the foreclosure proceedings, but holders should keep VA advised of their efforts to settle a disputed loss claim.

1.10 Escrow/Impound Account Maintenance (38 CFR 36.4346(e))

a. **Escrow/Impound Accounts.** Holders are not required to collect periodic deposits for tax and insurance or maintain a tax and insurance account but may do so if authorized under the terms of the security instruments. Holders must comply with the provisions of RESPA as administered by HUD.

b. **Disposition of Excess Balances.** An excess balance in the tax and insurance account should be disposed of as provided in the loan agreement and required by RESPA. With the consent of the borrower, VA will not object to applying the excess balance to delinquent installments. Similarly, and with the consent of the borrower, application of the excess to the principal balance or refunding it to the borrower would be acceptable

provided that no obligor is released from liability on the loan. On current accounts, if the borrower does not provide specific instructions for disposition of a surplus, it may be remitted directly to the borrower.

1.11 Servicing Transfers (38 CFR 36.4346(d))

Lenders or holders are not required to notify VA of, or obtain VA approval for, servicing transfers or sub-servicing transfers. It is recommended, however, that VA be given notice on active delinquencies (cases on which a notice of default has been filed) so that follow-up on these cases is maintained. In servicing transfer cases, the transferee will be held responsible for any failure of the transferor to comply with VA requirements (other than those discussed in par. 6.06 which are not applicable to a holder in due course) which would subject the claim to adjustment. Both the releasing and acquiring holder/servicer must comply with the disclosure and notification requirements of RESPA as administered by HUD.

1.12 Release of Security (38 CFR 36.4324)

a. **General.** VA will be released from all liability as guarantor if (1) a holder releases a portion of the security from the lien without VA's prior approval, and (2) the obligor is released from personal liability on the entire indebtedness. Even if an obligor is not released from liability, a claim may be reduced if a portion of the security was released without following the guidelines below.

b. **Prior VA Approval Not Required.** Holders may approve partial releases of security without VA's prior approval if all of the following conditions are met:

(1) The release did not involve a decrease in value of the security in excess of $2,500;

(2) The consideration received for the release is commensurate with the fair market value of the property released;

(3) The entire consideration is applied to the indebtedness;

(4) The aggregate amount of the release does not exceed $2,500; and,

(5) Any release or substitution of security is reported to the appropriate VA regional office within 30 days after completion of the transaction.

c. **Other Releases**

(1) All other releases must have the prior approval of VA. The request for approval should be submitted to the appropriate VA regional office and should contain:

(a) A letter of request from the current owner signed by all interested or obligated parties to the loan, such as the original veteran and secondary lienholders. An explanation must be provided if any person liable on the loan does not sign the request.

(b) A survey or sketch of the entire parcel showing clearly the portion to be released, the dimensions of the parcels, and the locations of all improvements.

(c) The status of loan, including the current unpaid principal balance and whether the loan payments are current.

(d) The consideration, if any, to be received for the property.

(e) The details of the intended disposition of funds, if consideration is not going to be applied to the indebtedness.

(f) Any available indication of the value of the property being released.

(g) A statement from the borrower agreeing to pay for the cost of an appraisal or survey if VA determines one is necessary.

(2) In general, the consideration received for the release must be at least equal to the reasonable value of the security released. If the entire consideration is not used to reduce the indebtedness, the ratio of loan balance to the remaining security must be adequate to protect VA against possible future loss in case of liquidation of the remaining security. VA will generally consider a loan-to-value ratio of 75 percent or lower to be adequate.

(3) Depending on the factual situation, VA may order a land survey of the property and/or an appraisal showing the reasonable value before and after the partial release to be made. The persons requesting the release will be required to pay the expense of the appraisal and/or land survey whether or not VA approves the request.

(4) VA will advise the holder by letter of the decision and give notice of any conditions required for approval of the request for release.

1.13 Loan Assumptions and Release of Liability--Loans Made Prior to March 1, 1988

a. Right to Sell

(1) The owner of property that is security for a VA loan for which a commitment was made prior to March 1, 1988, has the right to sell the property on any terms. No restriction, charge or fee may be imposed by a holder or its servicing agent that would limit or nullify this right.

(2) An exception applies when the loan was made by a State, territorial, or local governmental agency and the law requires acceleration of maturity of the loan upon sale or conveyance of the security property to a person ineligible for assistance. VA has approved due-on-sale clauses to allow veterans to participate in certain programs that require them to allow veterans to take advantage of below-market interest rates or other benefits.

b**. Fees.** VA does not approve fee charges for recording change of ownership of the mortgaged property. However, holders may charge up to $50 for amending their records to reflect a change in ownership, if the parties involved agree and it is permissible under the loan agreement.

c**. Liability of the Veteran.** The original mortgagor remains liable on the mortgage indebtedness unless he or she is released from personal liability. Under Federal law and VA regulations, the original veteran-borrower is obligated to indemnify the Government for any amount VA is required to pay the holder under the contract of guaranty. (For loans closed after December 31, 1989, however, veterans will not be required to reimburse the Government for claim payments except when evidence of fraud, misrepresentation or bad faith in connection with the loan origination or default is found.) This indemnity obligation is in addition to any rights VA may acquire by subrogation from the holder. VA encourages holders to include language on pay-off statements which reminds veterans of their liability and recommends that they obtain a release of liability from VA before permitting a loan assumption.

d**. Requirements for Release of Liability**

(1) Upon application made by a veteran and the transferee, VA will release the veteran from liability to the Government on the loan if the following three conditions are met:

(a) The loan is current;

(b) The purchaser qualifies as an acceptable credit risk; and,

(c) The purchaser assumes the veteran's loan obligations and liability (including the veteran's indemnity obligation), as evidenced by a written agreement in the form required by the VA office of jurisdiction or one that is found to have the same legal effect.

(2) The party assuming the loan need not be a veteran. A veteran may take advantage of this procedure regardless of whether the house was sold at a profit. The veteran's release also applies to the spouse.

e**. Effects on Holder.** A holder is not required to release the veteran from liability to it. The veteran's release from liability to VA will not affect the holder's rights to proceed against the veteran or affect the holder's contract of guaranty.

f. **Processing of Applications.** A release of liability must be processed by the VA office having jurisdiction over the loan. Holders will be requested to supply certain information, such as the current status of the loan, during the processing.

g. **Notice to Holders.** Generally, the loan holder will not be notified that a release had been granted unless notice was specifically requested. VA began to provide holders with copies of the obligor's release notification letter in mid-1993.

1.14 Loan Assumptions and Release of Liability--Loans Committed On or After March 1, 1988

a. **Limited Assumability.** Assumptions of loans for which loan commitments were made on or after March 1, 1988, must have the prior approval of VA or a VA automatic lender. With the exception of assumptions processed under the "special approval by VA" procedure described in subparagraph f below, approval of an assumption of a loan releases the veteran from liability to VA. The security instruments are required to carry a statement, in large type, that the loan may not be assumed without VA's prior approval. Failure to secure approval could lead to the acceleration of the loan after the transfer. Assumptions and releases of liability are generally processed by holders and include a funding fee and processing charge.

b. **Funding Fee** (38 CFR 36.4312(e))

(1) Funding fee equal to one-half of 1 percent of the loan balance as of the date of transfer must be paid by the transferee to the loan holder or its agent, at the time of transfer. The following are exempt from paying the funding fee as an assumer:

(a) A veteran receiving VA compensation for a service-connected disability;

(b) A veteran who, but for receipt of military retirement pay, would be entitled to receive compensation; and,

(c) A surviving spouse of a veteran who died in service or from a service-connected disability.

(2) See VA Pamphlet 26-7, Lender's Handbook, chapter 6, section II, for more information on exemptions from the funding fee and acceptable documentation.

(3) The holder should list the funding fee amount in every assumption statement provided and include a notice that the fee must be paid to the holder immediately following loan settlement.

(4) The holder must send the fee to the Secretary of Veterans Affairs within 15 days of the receipt by the holder of the notice of transfer. Transmittal of the funding fee to VA must be completed in accordance with VA Pamphlet 26-7, Lender's Handbook, chapter 6,

section II. The loan amount (item 10) on the transmittal form (VA Form 26-8986, Loan Guaranty Funding Fee Transmittal, see fig. 1-1) will be the balance of the loan assumed by the new owner rather than the original loan balance. However, the date of loan closing (item 9) will be the date the loan originally closed, not the transfer date.

c. **Processing Charge.** (38 CFR 36.4312(d)(8)) The maximum charge for processing an assumption application and changing the loan records is the lesser of:

(1) $300 plus the actual cost of any credit report required; or,

(2) Any maximum prescribed by applicable State law.

A holder may collect this charge in advance, including a reasonable estimate for the cost of the credit report, and then refund the portion allocable to a records change ($50) if the transfer is not completed. A charge of $50 is for underwriting the assumption. If VA is underwriting, the $50 charge cannot be assessed or must be refunded. VA does not specifically regulate when the $300 charge may be assessed; however, since borrowers or brokers may request an assumption package before a sales contract has been signed, it is recommended that holders require that the fee accompany the completed package rather than requiring it as a condition for mailing the forms to a requester.

d. **Processing of Assumptions - Automatic Lenders** (38 CFR 36.4303(k)(1))

(1) **Responsibility.** If both the holder and its servicing agent are automatic VA lenders, they must decide which one will make the determinations described below. If the actual loan holder does not have automatic authority and its servicing agent is an automatic lender, the servicing agent must make the determinations for the holder. The holder will remain responsible for any failure of its servicing agent to comply with the applicable law and VA regulations.

(2) **Processing and Underwriting.** If the seller applies for approval of the assumption prior to completing the sale, a holder or its authorized servicing agent who is an automatic lender must examine the application to determine compliance with the following provisions of 38 U.S.C. 3714:

(a) The loan is current (or will be brought current at the closing of the sales transaction).

(b) The prospective purchaser of the property is creditworthy. The creditworthiness review must be performed by the party that has automatic authority and must be conducted in accordance with 38 CFR 36.4337 and VA Pamphlet 26-7, Lender's Handbook, Chapter 5, Section II.

(c) The prospective purchaser has agreed to assume all of the loan obligations, including the obligation to indemnify VA if a claim is paid.

(3) **Timeliness Requirements.** The holder must complete its examination and advise the seller of its decision no later than 45 days after the holder receives a complete application package for approval of an assumption. The 45-day period may be extended by the amount of time lost to delays documented as beyond the control of the holder, such as employers or depositories not responding to requests for verifications or follow-ups on requests.

(4) **Approval Notices.** When advising the seller that the assumption has been approved, the holder should include instructions for the assumption of liability (see subpar. b below) and the amount of funding fee which will be payable. After the transfer is completed, the holder must send VA:

(a) The credit package containing an application, loan analysis, credit report, verifications of income and deposits, and other pertinent information used to support the income and credit determination. If this information was previously submitted in connection with an appeal, it will not be necessary to send duplicate copies.

(b) A copy of the executed deed and/or assumption agreement as required by the VA office of jurisdiction. Requirements for assumption of liability to a loan holder and to VA will vary according to local law. Each VA regional office has prepared for each State under its jurisdiction an information package describing the usual requirements for assumption of liability, as well as procedures to follow for unusual cases. Holders should obtain a package for each State in which they do business.

(c) A certification by the holder's or servicer's VA-approved underwriter that the assumption complies with the applicable law and regulations.

(d) A copy of the VA receipt for the assumption funding fee.

(5) **Disapproval Notices.** If the application for assumption is disapproved, the holder must notify the seller and the purchaser that the decision may be appealed to VA within 30 days. When a case is appealed to VA, the holder must provide VA all items it used in making its decision. If the application remains disapproved after 60 days (to allow time for appeal and review by VA) the holder must refund $50 if it previously collected any processing charge, because there will be no need for a records change.

(6) **Appeal to VA.** If the assumption is approved on appeal, VA will notify the seller and loan holder. If it is not approved, VA will notify the seller and holder and advise the seller of the right to request "special approval" within 15 days of receipt of the disapproval notice.

e**. Processing of Assumptions - Holders and Servicers Without Automatic Authority** (38 CFR 36.4303(k)(1)(ii))

(1) **Usual Processing.** If neither the holder nor its authorized servicing agent is an automatic lender, and the seller applies for approval of the assumption prior to completing

the sale, the holder or its agent must develop a complete credit package for VA to determine the creditworthiness of the purchaser. This package must be sent to VA along with a copy of the purchase contract and information as to whether the loan account is current or in default.

(2) **Timeliness Requirements.** Documents must be submitted to the VA regional office of jurisdiction no later than 35 days after the date the holder receives a complete application package, subject to the same extensions for documented delays previously described for automatic lenders in subparagraph d(3) above. If VA advises that a proposed assumer is creditworthy and the transfer is completed, the holder will be required to timely submit the appropriate documentation to VA (see subpar. d(4) above), although the certification will not require the signature of an underwriter, and will state only that the application for assumption approval was processed in accordance with the applicable law and regulations.

(3) **Processing Charge and Refunds.** If the maximum processing charge of $300 was collected with an application for assumption approval (based on the possibility that a firm may be servicing loans for holders with and without automatic authority) and the credit package must be referred to VA for the underwriting decision, then $50 of the maximum charge must be refunded. If VA does not approve the application or if the appeal is denied, the holder will be notified and an additional $50 of the processing charge must be refunded following the expiration of the 30-day appeal period because this amount will not be needed to complete a records change.

f**. Special Approval by VA.** Within 15 days of receipt of the disapproval notice, the seller may request "special approval" from VA. VA may determine "special approval" is in the best interest of the Government if:

(1) The transferor agrees to remain secondarily liable on the loan following assumption,

(2) The transferor is unable to otherwise continue payments on the loan, and

(3) Reasonable efforts have been made to find a creditworthy buyer for the property.

If approved, VA will provide notice to the transferor and the loan holder that the assumption has been approved and that he or she will not be released from liability to VA. The "special approval" by VA does not include approval for the loan holder to release any obligor from liability. If an obligor is released by the loan holder without VA's prior approval, VA may be released from further liability on the guaranty.

g. **Transfer Without Prior Approval.** (38 CFR 36.4303(k)(2)) The holder must notify VA within 60 days after learning of a transfer that did not receive prior approval of VA or an automatic lender. The notice must advise VA whether the holder intends to exercise its option to immediately accelerate the loan or whether the transferor and transferee will be given the opportunity to apply for "retroactive approval" of the

assumption. In this context, the phrase "acceleration of the loan" means referral to an attorney to initiate foreclosure.

(1) **Review of Purchaser's Liability.** Upon learning of an unapproved transfer, a holder may decide to demand immediate payment of the one-half of one percent VA funding fee and request a copy of the instrument of transfer to determine the liability of the purchaser.

(a) **Liability Assumed.** If the purchaser pays the funding fee and has assumed all of the seller's obligations in the transfer deed (and if the assumption language is legally binding), then it would appear that the purchaser intends to satisfy those obligations and an opportunity for retroactive approval of the transfer probably should be afforded.

(b) **Liability Not Assumed**. If prior approval of a transfer was not obtained and the title transferred "subject to" the mortgage or deed of trust, then the purchaser usually has no liability on the loan. Such a purchaser may have no incentive and little intention of maintaining the payments. It may still be advisable to extend the opportunity to apply for retroactive approval of the transfer, with the expectation that the purchaser will assume liability for repayment of the loan.

(2) **Retroactive Approval Processing.** If an opportunity to apply for retroactive approval is granted, processing will be completed in the same manner as if the application had been received prior to the transfer, including the right of appeal to VA.

(3) **Consideration of Loan Acceleration.** Should a purchaser fail to cooperate in the retroactive approval process, then acceleration of the loan may or may not be advisable, depending upon the implications under State law of delaying acceleration, as compared to the prospect of accelerating a current loan which has the potential for future timely payments.

h. **Release of Liability.** (38 CFR 36.4323(h)) When an application for assumption is approved (either by VA or the loan holder or servicer) and the transfer is completed with the purchaser assuming all of the seller's liability on the loan and to VA, the holder must release the seller of further liability to VA. This may be done in letter form if not a part of an assumption agreement, or if an agreement is not required. If it desires to do so, the holder is also authorized to release the seller from liability to the holder on the loan without separate approval from VA. This does not apply if the seller has agreed to remain liable and has obtained "special approval" for the assumption from VA.

i**. Unrestricted Transfers.** (38 CFR 36.4308(c)(1)) Certain transfers of ownership otherwise subject to 38 U.S.C. 3714 do not require prior approval of the holder, as described below. A loan may not be accelerated due to these types of transfers, and a release of liability will not be processed by the holder. Application for release of liability on unrestricted transfer cases must be processed by VA. The processing charge and funding fee may not be collected. However, a reasonable fee up to $75 may be charged

for changing the holder's account records, provided it is agreed to by the parties or is permissible under the loan agreement.

(1) The creation of a lien or other encumbrance subordinate to the lender's security instrument which does not relate to a transfer of rights of occupancy in the property;

(2) The creation of a purchase money security interest for household appliances;

(3) A transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

(4) The granting of a leasehold interest of 3 years or less not containing an option to purchase;

(5) A transfer to a relative resulting from the death of a borrower;

(6) A transfer when the spouse or child of the borrower becomes a joint owner of the property with the borrower;

(7) A transfer resulting from a decree of a dissolution of marriage, legal separation agreement, or from an incidental property settlement agreement by which the spouse of the borrower becomes the sole owner of the property. In such a case, the borrower has the option of applying directly to the VA regional office of jurisdiction for a release of liability under 38 U.S.C. 3713(a); or

(8) A transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property.

j**. Sale Agreements Not Subject to 38 U.S.C. 3714.** A sale on an installment contract, contract for deed, or similar arrangement in which title is not transferred from the seller to the buyer is not considered a "disposition" of property and therefore does not require prior approval by VA or the loan holder. However, the holder should caution any borrower considering a sale in this manner that he or she remains liable for repayment of the loan under such an arrangement.

(1) **Loan Records**. Even if the agreement calls for the contract purchaser to make payments directly to the loan holder, the holder is not required by VA to change its records, and the contract seller is responsible for forwarding payment coupons and other information to the contract purchaser. Depending on the circumstances of a case, a holder may agree to change the account address to read in care of the contract purchaser, although the contract seller must promptly advise the holder of any change in his or her address.

(2) **Eventual Title Transfer on Contract Sales**. Sales by installment contracts typically call for transfer of title after a certain period of time. If the contract calls for title to transfer prior to payment in full of the VA loan, assumption approval will be required,

and processing charges and VA funding fees will be applicable upon transfer. The borrower should be advised to include as one of the conditions of the contract that application for assumption approval be made, and approval secured, prior to the completion of title transfer. The contract should then address the options of both parties if the request for assumption approval is disapproved. Among the options could be voiding the contract with forfeiture of all payments previously made, or an extension of the contract period to allow the purchaser to correct any credit deficiencies and apply for approval at a later date.

k. **Substitution of Entitlement.** VA will continue to process the substitution of entitlement on assumption cases, although this will usually be done only after a holder has provided notice of an approved transfer. If a review of the sales contract indicates it is contingent upon restoration of VA benefits, or if a question about the possibility of substitution of entitlement arises, the seller should be referred to the VA office of jurisdiction. To complete a substitution, the buyer must have sufficient entitlement to substitute for that of the seller, and this information can usually be obtained only from VA. In addition, the veteran-buyer must certify that the property securing the loan will be occupied as his or her home using VA Form 26-8106, Statement of Veteran Assuming GI Loan (Substitution of Entitlement). In some cases, VA Form 26-8320, Certificate of Eligibility for Loan Guaranty Benefits, may be valid only if the veteran provides a certification that he or she has not been released from active duty at the time a loan is obtained or assumed.

l. **Transmittals to VA.** Appendix C provides detailed instructions on origination loan file setup for prior-approval applications and closings, and for automatic loans. The same order is appropriate in providing items required by the various types of notices which will be submitted on assumption approvals and releases of liability. Processing at VA will be expedited if holders include a cover letter identifying it as a completed transfer, a request for approval by VA, or information on an appealed case. The cover letter should also identify the VA loan number, original veteran, and the name and telephone number of a contact person at the holder/servicer. Any indication of a request for substitution of entitlement should also be noted.

1.15 Soldiers and Sailors Civil Relief Act

a. The Soldiers and Sailors Civil Relief Act of 1940, as amended (50 USC App. sections 501-590) provides for a loan interest rate cap of 6 percent and other relief for veteran-borrowers called to active military service on loan obligations incurred prior to their current period of service. Foreclosures must be approved by the court. If a claim is filed, VA will not include interest on the obligation in excess of 6 percent for the period of time the veteran was eligible for the rate reduction provisions of the Act.

b. Appendix D, Circular 26-90-32, provides more information about the Act. Holders are advised to consult counsel to ensure compliance with all provisions of the Act as well

as any local statutes that may require the extension of forbearance. VA does not administer the Act.

1.16 Loans Paid in Full (38 CFR 36.4333)

Upon full satisfaction of a guaranteed loan by payment or otherwise, the holder must return the certificate of guaranty to VA marked canceled. If the certificate is not available, the holder must still inform VA in writing that the loan has been paid in full.

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CHAPTER 2. DELINQUENT SERVICING

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CHAPTER 2. DELINQUENT SERVICING

2.01 System for Servicing Delinquent Loans (38 CFR 36.4346(f))

VA has a keen interest in delinquent loan servicing both because of the Government's financial obligation as guarantor and because of the responsibility to provide assistance to veterans. Holders must have a system for servicing delinquent loans which ensures that prompt action is taken to collect amounts due from borrowers and minimizes the number of loans in default. The holder's servicing system must include the following:

a. An accounting system that promptly alerts servicing personnel when a loan becomes delinquent.

b. A collection staff trained in the techniques of loan servicing and counseling delinquent borrowers about:

(1) How to cure delinquencies;
(2) Protecting their equity and credit rating; and,
(3) Alternatives to foreclosure.

c. Procedural guidelines for the individual analysis of each delinquency.

d. Instructions and controls for:

(1) Sending delinquent notices;
(2) Assessing late charges;
(3) Handling partial payments;
(4) Maintaining servicing histories; and,
(5) Evaluating repayment proposals.

e. Management review of collection efforts and borrower response prior to a decision to start liquidation.

f. Procedures for reporting delinquencies of 90 days or more and loan terminations to major credit bureaus and for informing borrowers that such action will be taken. (VA does not object to reporting delinquencies earlier or to full file reporting.)

g. Controls to ensure that required notices are sent to VA on time and in the proper form.

2.02 Collection Actions (38 CFR 36.4346(g))

Holders should employ collection techniques which are flexible enough to adapt to the individual needs and circumstances of each borrower. A variety of collection techniques may be used, although the holder's collection procedures must at least include the following:

a. **Delinquent 17 Days.** If a loan installment has not been received within 17 days after it is due, the borrower must be sent a written delinquency notice requesting immediate payment. The notice must be mailed no later than the 20th day of the delinquency and must state the amount of the payment and of any late charges that are due.

b. **Telephone Contact.** Concurrent with the delinquency notice (in any event, no later than the 30th day of the delinquency), an attempt should be made to contact the borrower by telephone to determine why payment was not made and to emphasize the importance of remitting loan installments as they come due.

c. **Delinquent 30 Days.** If telephone contact has not been made, a second letter, preferably personally worded, must be sent to the borrower. The letter should:

(1) State that the loan is in default.

(2) Emphasize the seriousness of the delinquency and the importance of taking prompt action to resolve the default.

(3) Report the total amount due.

(4) Advise the borrower how to contact the holder to make arrangements for curing the default.

d. **Face-to-Face Interview.** A reasonable effort to arrange a face-to-face meeting must be made if the holder has not established contact with the borrower and has not determined the borrower's financial circumstances or established a reason for the default or obtained the borrower's agreement to a repayment plan before the default is reportable to VA. Services of a third party, such as a property inspection contractor, may be obtained for this purpose. Holders have the option of authorizing a third party contractor to perform all, or some, of the servicing actions outlined in paragraph 2.03 or restricting them to referring the borrower to the holder's office for completion of a servicing interview.

e. Failure to Perform. The holder must explain any failure to perform these collection actions when reporting loan defaults to VA.

2.03 Conducting Interviews with Delinquent Borrowers (38 CFR 36.4346(h))

When personal contact with the borrower is established, the holder should solicit enough information to evaluate the prospects for curing the default and to decide whether forbearance or other relief assistance would be appropriate. At a minimum, the holder must make a reasonable effort to establish the following:

a. The reason for the default and whether the reason constitutes a temporary or permanent condition;

b. The borrower's present income and employment;

c. The current monthly expenses of the borrower, including all household and debt obligations;

d. The borrower's current mailing address and telephone number; and,

e. A realistic and mutually satisfactory arrangement for curing the default.

2.04 Property Inspections (38 CFR 36.4346(i))

a**. When to Inspect.** The holder should make an inspection of the mortgaged property whenever it becomes aware that its physical condition may be in jeopardy. Unless a repayment agreement is in effect, a property inspection must also be made at the following times:

(1) Before the 60th day of delinquency or before initiating action to liquidate a loan (i.e., referring the case to an attorney to begin foreclosure), whichever is earlier;

(2) At least once each month after liquidation proceedings have been started, unless servicing information shows the property remains owner-occupied.

A reasonable fee for property inspections required by VA may be charged to the borrower if permitted by the loan instruments and included in a claim filed with VA if the account is not reinstated. VA should be notified in writing if any damage to the property is found (the notice of default may be used for this purpose if one has not yet been filed when the damage is found; otherwise, a letter or memorandum should be sent).

b**. Abandonment.** When a holder obtains information that a mortgaged property is abandoned, it should make appropriate arrangements to protect the property from vandalism and the elements. Thereafter, inspections should be scheduled at least monthly to prevent unnecessary deterioration due to vandalism or neglect. For any loan more than 30 days delinquent, a property abandonment must be reported to VA and appropriate

action (i.e., referral to counsel to initiate foreclosure) initiated within 15 days after the holder confirms the property is vacant. See paragraph 4.06 for instructions on filing VA Form 26-6850a, Notice of Default and Intention to Foreclose. VA can waive this requirement if there is reason to believe the account will be reinstated. Reasonable judgment should be exercised in considering all circumstances--property condition, for sale signs, date of last payment received, presence of personal property or vehicles, yard condition, owner's mailing address, etc.--and arriving at a conclusion as to whether a property is abandoned or temporarily vacant.

2.05 Collection Records (38 CFR 36.4346(j))

Individual file records of collection action on delinquent loans must be maintained and made available to VA for inspection on request. Paper files, database records, or any combination are acceptable, as are designations used to identify standardized form letters and notices. The collection records must contain:

a. The dates and content of letters and notices which were mailed to the borrower(s);
b. Dated summaries of each personal servicing contact and the results;
c. The indicated reason for default; and,
d. The date and result of each property inspection.

This information must be reported on the notice of default and the notice of intention to foreclose forms.

2.06 When and How to Report the Default (38 CFR 36.4315(a))

a**. General**. The holder must notify the VA office of jurisdiction within 45 days after a borrower is in default:

(1) By reason of nonpayment of any installment for 60 days from the date of first uncured default; or,

(2) By failing to comply with any other covenant or obligation of the loan for a continuing period of 90 days after demand for compliance has been made. Nonpayment of real estate taxes do not need to be reported until the failure to pay when due has persisted for 180 days.

The NOD (VA Form 26-6850, Notice of Default), should be used to report the default. For nonpayment default, VA must be in receipt of the NOD within 105 days of the date of the first uncured default. Failure to report timely could lead to an adjustment of any claim under guaranty. (38 CFR 36.4325(b))

b. Assumptions

(1) For loans closed based on commitments issued after March 1,1988 (which cannot be assumed without prior approval), VA must be notified on VA Form 26-6850 within 60 days after the holder learns of an unapproved change of ownership.

(2) For older loans which can be assumed without prior approval, an NOD should be filed within 15 days after two installments are due and unpaid, if an assumption took place less than 12 months before the date of first uncured default. (Early reporting in these cases is not mandatory, but is strongly recommended because it can reduce losses caused by transfer of property to equity skimmers or unqualified buyers.)

c. **Abandonments.** VA Form 26-6850a should be used if the property is abandoned or if it is determined that the default is insoluble before the NOD has been filed. Abandonments, as well as cases when the default is determined to be insoluble before 60 days have elapsed from the date of first uncured default, should be reported promptly. NOTE: 38 CFR 36.4346(i) requires holders to begin action under 38 CFR 36.4317(a) within 15 days after confirming a property is abandoned. If the loan is in default, VA will construe "appropriate action" under the regulation as referral of the case to counsel for initiation of foreclosure. While the regulations do not specifically require that a notice of default be filed under these circumstances, VA asks holders to do so, using VA Form 26-6850a.

d. **Cures.** If the loan was previously in default but has been reported cured, a new NOD must be filed. If there is any question as to whether a cure was reported, a new NOD should be filed to avoid the risk that a subsequent claim will be adjusted for failure to report the default timely. VA will treat the NOD as a status update if no cure has been processed.

2.07 VA Form 26-6850, Notice of Default

An example of a properly completed NOD appears in figure 2-1. In filling out the NOD, holders should pay special attention to the following:

a. **VA LIN (VA Loan Identification Number)**. The VA LIN must be numeric and 12 digits in length. Many VA loan numbers in holders' records have less than twelve digits because of the way they were assigned by the VA regional office of jurisdiction. They should be converted to the correct VA LIN in accordance with the instructions in appendix B.

b. **Holder's and Servicing Agent's Phone Number**. A specific, direct line, telephone number enables VA loan service representatives to contact the proper specialist in the holder's servicing department when discussion of a case is necessary.

c. **Date of First Uncured Default (Item 2)**. This is the due date of the first or earliest partially or fully unpaid installment.

d. **Present Owner's Social Security Number (Item 3A)**

e. **Present Owner's Telephone Number (Items 17E and 17F)**. A diligent effort should be made to obtain the telephone numbers for both the property owner's place of employment and home. If numbers are not available, note in the servicing summary what efforts have been made to obtain them. This will prevent duplication of effort when VA begins supplemental servicing.

f. **Original Veteran's Name and Present Address (Item 8)**. If someone other than the original veteran is the present owner, the name and current address of the original veteran should be provided. For purposes of the NOD, the original veteran's name is required by 38 CFR 36.4332; his or her current address should be the most recent available in the holder's system of records (after a notice of intention to foreclose is filed, holders must make an effort to determine the original veteran's current address--see par. 4.07). Because veterans may be held liable to reimburse the Government for claims paid due to transferee defaults, VA requires this information to try to provide veterans with notice of transferee defaults. In some areas, generally those in which foreclosure cannot be completed quickly, it is not essential that VA have this information at the time the NOD is filed. Since many holders do not retain data on prior obligors in their automated servicing records, each VA office of jurisdiction has issued a release informing holders whether or not they must strictly adhere to this regulatory requirement.

g. **Reason for Default (Item 19)**. Usually there are reasons other than for default besides "improper regard." Check for curtailment of income, marital difficulties, illness or injury, extensive obligations, etc. Use item 19 if no contact has been made with the borrower and the reason for default is unknown.

h. **Summary of Loan Servicing (Item 20)**. It is very important that VA have complete information about the default and the prospects for resolution. Use the back of the NOD or separate sheet of paper if more space is needed. A narrative summary of any contacts made with the borrowers is helpful in evaluating the prospects of a loan reinstatement and for VA supplemental servicing. A copy of the in-house servicing record is acceptable as long as the VARO has been provided with instructions on how to read it and explanations of any abbreviations it contains.

i. **Signature (Item 22)**. The form must be signed by a corporate officer or other authorized full-time employee of the holder or its servicing agent. If the proper signature is omitted, the form will be returned for signature. The individual signing the notice should review the form to see that the information provided is accurate.

j. The NOD must include certification that the default has been reported to the credit bureaus.

2.08 Interim Loan Status Reports to VA

a. On loans reported in default, VA regularly produces a computer-generated VA Form 26-8778, Request to Lender for Status of Loan Account-LCS. This form should be completed and returned without delay. The information provided updates VA's records and assists in determining the viability of the loan. Failure to provide updates timely may result in the establishment of premature cut-off dates under 38 CFR 36.4319(f) and unnecessary telephone requests from VA for current information.

b. In completing the status update, use the servicing update/remarks section to advise VA of servicing efforts, contacts made, arrangements made with the borrower, or special occurrences such as bankruptcy. If additional space is required, use the reverse side of the form or an additional sheet of paper. As with an NOD, a copy of the in-house servicing record is acceptable as long as it can be understood by VA. Figure 2-2 is an example of a properly completed VA Form 26-8778.

c. Holders should notify VA as soon as possible when a default is cured or a repayment plan is arranged. It is not necessary to wait for a status request from VA or to use a specific VA form.

2.09 Partial Payments (38 CFR 36.4315(b))

A partial payment is a remittance on a loan in default of any amount less than the full amount due under the terms of the loan which are in effect when the payment is tendered.

a**. Acceptance of Partial Payments**

(1) The holder must accept any partial payment except as provided in subparagraph b below. The holder must either apply it to the borrower's account or identify it with the borrower's account number and hold it in suspense pending disposition. When partial payments held for disposition add up to the full monthly installment, including escrow, they must be applied to the borrower's loan.

(2) Partial payments should not be processed routinely unless they are remitted under the terms of a forbearance/reinstatement plan. When one is received, even if it must be accepted pursuant to the regulation, the holder should contact the borrower to find out why only a partial payment was remitted and arrange for payment of the balance due to cure the default.

b. **Return of Partial Payments.** A partial payment may be returned to the borrower only if one of the following conditions exists:

(1) The property is wholly or partially tenant-occupied and rental payments are not being remitted to the holder for application to the loan account;

(2) The payment is less than one full monthly installment, including escrow and late charge, if applicable, unless a lesser amount has been agreed to under a written repayment plan;

(3) The payment is less than 50 percent of the total amount then due, unless a lesser payment amount has been agreed to under a written repayment plan;

(4) The payment is less than the amount agreed to in a written repayment plan;

(5) The amount tendered is in the form of a personal check and the borrower has been previously notified in writing that only cash or certified remittances are acceptable;

(6) A delinquency of any amount has continued for at least 6 months since the account first became delinquent and no written repayment plan has been arranged;

(7) Foreclosure has been commenced with the first action required for foreclosure under local law;

(8) The holder's lien position would be jeopardized by acceptance of partial payment; or,

(9) The VA office of jurisdiction has given prior approval to return partial payments received on the account.

The payment must be returned within 10 calendar days from the date of its receipt, accompanied by a letter of explanation.

2.10 Bankruptcy and Other Legal Proceedings (38 CFR 36.4319)

When a holder initiates suit or otherwise becomes a party in any legal or equitable proceeding in connection with a guaranteed loan, copies of all procedural papers must be provided to the VARO of jurisdiction. Failure to do so may result in partial or total loss of guaranty. This includes bankruptcy, partition suits, foreclosure by second lien holders, condemnation notices, etc. VA must receive the notice in time to respond to the proceeding as if VA were a direct party to the action. Timely submission of bankruptcy notices is especially important because failure to do so may result in establishment of a premature cut-off date (under 38 CFR 36.4319(f)) by VA. Bankruptcy notices should include a copy of the schedule of creditors, when available, because this information is useful for evaluating prospects for reinstatement of the loan and may provide an insight into the accuracy of the loan or assumption application, especially in a loan default within the first 2 years of origination or an approved assumption, .

2.11 VA Supplemental Servicing

a. **Purpose.** The primary responsibility for servicing delinquent loans rests with the loan holder. However, an aggressive program of personal supplemental servicing is conducted by VA to ensure that each veteran-borrower is afforded the maximum opportunity to continue as a homeowner during periods of temporary financial distress. VA also attempts, through supplemental servicing, to minimize losses to the Government as a result of foreclosure.

b. **Servicing Process**

(1) Upon receipt of an NOD, VA automatically sends the borrower a letter describing the various options for reinstating the loan or otherwise avoiding foreclosure. A similar letter is sent after VA receives an NOI or NOD&I. Copies of these letters appear in figures 2-3 and 2-4.

(2) VA personnel will attempt to contact the veteran-borrower by telephone in most cases to reinforce the seriousness of the default and determine if there is any way to resolve it other than foreclosure. In many cases, VA will recommend a specific repayment plan for the borrower to propose to the holder. Occasionally, VA will contact the holder directly to request forbearance or acceptance of a repayment plan. The VA loan service representatives involved in supplemental servicing are experienced in loan servicing and will base proposals for forbearance, repayment plans or alternatives to foreclosure on a detailed analysis of the borrower's financial situation and motivation.

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CHAPTER 3. ALTERNATIVES TO FORECLOSURE

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CHAPTER 3. ALTERNATIVES TO FORECLOSURE

3.01 Delinquent Loan Servicing Policy

VA, through personal supplemental servicing and guidance to loan holders, expects every realistic alternative to foreclosure which may be appropriate in light of the facts in each case to be explored before a loan is terminated by foreclosure. VA loan holders should expect to be contacted at various times during the course of a default by VA loan service representatives to discuss the case and will frequently be requested to assist in pursuing a specific alternative. Since alternatives to foreclosure generally result in either reinstatement of the account or a faster termination than would be obtained through foreclosure, they also benefit loan holders by reducing the possibility that interest accrual and foreclosure costs will create a "no-bid." Alternatives to foreclosure should be discussed with borrowers by the holder as soon as possible in the course of the default, preferably before legal action is initiated, to obtain the borrower's cooperation and minimize the chances that resolution of the default will be delayed by bankruptcy.

3.02 Forbearance

a. **Encouragement of Forbearance**

(1) It is VA's policy to encourage holders to extend reasonable forbearance in the event a worthy borrower is unable to begin an immediate plan to liquidate the delinquency.

(2) Forbearance is granted by allowing payments to remain delinquent for a reasonable time (usually not more than 12 months), to be followed by reinstatement of the loan through payment of a lump sum or a schedule of increased payments. For the typical default, a certain amount of forbearance is built into VA's default reporting requirements because the default may not be reported until 60 days after the date of first uncured default and foreclosure may not be initiated for 30 days after an NOI is received by VA. At any time in the servicing process, and especially once an NOD has been filed, holders should, as a matter of prudent servicing, obtain a written agreement with the veteran regarding the payment of the delinquency before granting forbearance beyond that which is built into VA's reporting requirements. The lack of a written agreement does not, however, prevent the holder from extending forbearance when it appears appropriate. The holder should inform VA of the forbearance and the reasons for it in the NOD and status updates. This information assists VA's supplemental servicing activity and can prevent the establishment of an inappropriate cutoff date.

b. **Predetermination of Net Value.** The holder may request an assurance from VA that should foreclosure become necessary VA will specify an amount at the foreclosure sale despite any decrease in value or increase in indebtedness that occurs during the period of forbearance. This predetermination of net value can only occur if:

(1) Foreclosure is imminent; and,

(2) The holder is willing to extend forbearance for a fixed period of time but is concerned that in the event of foreclosure VA may not specify an amount, which would expose the holder to a loss that would have been avoided by a prompt foreclosure.

Under these circumstances VA will make a net value determination, taking into account the period of forbearance, and advise the holder whether VA would specify an amount in the event of foreclosure.

3.03 Modifications-Extensions and Reamortizations (38 CFR 36.4314)

a. Modification involves a change of any of the terms of the original security instrument. Modification should be considered when the borrower's income has been curtailed and the borrower is financially unable to either maintain the payment at the current amount or to make up the delinquent payments, but will be able to keep the loan current after modification. Paragraph 1.06 discusses policies and procedures for extending or reamortizing a loan.

b. If the holder finds that modification is appropriate, but for some reason is unable to extend or reamortize the loan itself, it should notify VA so that refunding of the loan can be considered promptly (see par. 3.06). Refinancing a higher interest rate loan at a current, lower rate under VA's interest rate reduction refinancing program is also recommended in such cases. If the loan is current, no underwriting is necessary; if the loan is delinquent, VA can expedite prior approval of an application.

3.04 Sale of Property and Compromise Agreement

a. **Encouraging Sale of Property.** When borrowers are unable to maintain their mortgage payments, they should be encouraged to sell their homes at realistic prices to avoid foreclosure and salvage any equity they may have. Early counseling with borrowers about private sale can often help avoid loan terminations and reduce or eliminate losses to all interested parties. When the borrower has equity in the home, the holder should grant the borrower forbearance of reasonable duration to permit a sale.

b. **Proceeds Not Sufficient to Pay Indebtedness.** In some cases, because the property has declined in value or has not appreciated enough to cover repayment of a delinquency and the costs of sale, a private sale cannot take place without additional funding. VA will consider providing a "compromise claim" payment if an offer to purchase the property is received but the proceeds will not be sufficient to pay off the loan or to pay the delinquency in the case of an assumption. The sales price of the property should be the fair market value. In some assumption cases, where the fair market value is less than the unpaid principal balance of the loan, VA's compromise claim payment will also include funds to be applied as a prepayment to principal to reduce the loan balance to the amount

the purchaser has agreed to assume. Any purchaser assuming a VA loan involving a compromise claim must be found by VA to be an acceptable credit risk and must agree to assume full legal liability for repayment of the loan and to indemnify VA against loss in the event of a future default. If the sale is approved, VA will pay the holder a compromise claim for the difference between the net sales proceeds and the mortgage balance.

c. **VA Approval**

(1) VA must approve each compromise sale in advance. VAROs will generally require the following information prior to considering a compromise sale:

(a) A copy of the signed offer to purchase. The offer should include a contingency clause which reads, "This offer is contingent on VA approval of a compromise agreement."

(b) Estimated closing date.

(c) Statement of projected settlement costs.

(d) VA Form Letter 26-567, Status of Loan Account - Foreclosure or Other Liquidation.

(e) An appraisal or broker's estimate of value.

(f) If the loan is being assumed, a release of liability package must be completed by the seller and purchaser and submitted to the VA office of jurisdiction. Only VA, on a prior approval basis, can process an assumption and release of liability in cases involving compromise claim payments.

(2) VAROs will notify the holder and borrower when a compromise offer is tentatively approved and list the conditions of final approval. Generally, tentative approval is granted when the purchaser is determined to be acceptable from a credit standpoint and final approval is contingent upon execution of proper documents by the purchaser which evidence his or her legal liability to VA and for repayment of the loan. The notice will contain any necessary instructions regarding documentation and claim payment procedures.

d. **Compromise Claim**

(1) After the sale of the property has closed, the holder may claim payment from VA for the shortage as agreed. The following documentation is generally required to obtain payment. The VA regional office of jurisdiction will provide specific instructions.

(a) A certified statement of account (in effect, a certified copy of the ledger sheets or equivalent showing the amounts and dates of all debits and credits to the account).

(b) VA Form 26-1874, Claim Under Loan Guaranty, if required by the VARO. See paragraph 6.02 for more information on completing the form.

(c) Invoices for attorney fees and property preservation expenses.

(d) A copy of the settlement statement (HUD-1).

(e) A signed promissory note if the veteran is being required to repay VA for all or part of the compromise claim. (Some VAROs will obtain this independently; others require the holder to obtain it.).

(2) If the loan is being assumed, the following are also required:

(a) A copy of the recorded transfer deed and/or assumption agreement as required by the VA office of jurisdiction.

(b) The original guaranty certificate, which will be changed to reflect the claim payment and returned to the holder. (If the guaranty certificate is not available, or cannot be obtained from the document custodian, notify the VARO before proceeding with the sale so that alternative arrangements can be made.)

3.05 Deed in Lieu of Foreclosure (Voluntary Conveyance)

a. **General**

(1) When it is concluded that there is no alternative to terminating the loan, and a voluntary conveyance can be accomplished more quickly than a foreclosure, holders are strongly encouraged to explore the possibility of a deed in lieu of foreclosure.

(2) A voluntary conveyance may not be accepted without VA prior approval.

(3) Obtaining the deed must be legally feasible and the borrower must be willing to cooperate. A deed in lieu will usually not be accepted if there are any junior liens on the property. If the value of the property is substantially in excess of the debt, the borrower should be encouraged to sell the property rather than offer a deed. If the net value of the property does not exceed the unguaranteed portion of the indebtedness (which would result in a no-bid in the event of foreclosure, see par. 4.13), a voluntary conveyance will normally not be approved. In such cases, however, VA may approve a voluntary conveyance after the holder completes a partial debt waiver or reduction. If the holder does not intend to complete a partial debt waiver or reduction, VA may authorize the holder to accept a voluntary conveyance with no right to reconvey the property to VA. Such authorization is limited to cases when the borrower either will not be legally liable to reimburse VA for the claim paid or lacks the financial resources to do so.

b. **Consideration**

(1) The consideration for a deed in lieu of foreclosure is often a full and complete release of the mortgagor's personal liability. This should provide sufficient incentive for the borrower to execute the deed and also preclude any title questions.

(2) For legal purposes, avoidance of a recorded foreclosure and reduction of the liability amount may be a sufficient consideration. In some instances, where a complete release of liability is not required by law or necessary to remove any potential cloud on title, the borrower may be required to agree to repay VA for all or part of the claim paid.

c. **VA Approval**

(1) The acceptance of a voluntary conveyance requires VA's prior approval. The holder should notify borrowers in writing that a deed in lieu of foreclosure is not acceptable until approved by VA. Borrowers should be advised to provide the loan holder with:

(a) A signed financial statement showing their assets, liabilities, income and expenses. (VA Form 26-6807 may be used.)

(b) A written statement requesting a deed in lieu of foreclosure and advising the reason for default, explaining why it is necessary to give up the security property and what efforts have been made to dispose of it, and an agreement to vacate the property when the deed is recorded or to give possession of the property to VA immediately upon notification to do so.

(2) Upon receipt of the borrower's financial and written statements, the holder should forward them and the following documentation to the VARO of jurisdiction.

(a) VA Form 26-6851, Notice of Intention to Foreclose, if not previously filed, indicating that a deed in lieu is obtainable.

(b) A statement of account (VA Form Letter 26-567).

(c) Occupancy status. If occupied, the name and telephone number of the occupant. If vacant, the keys properly identified with the VA LIN and property address.

(d) Title status. If information about any liens on the property which could affect the decision to accept a voluntary conveyance is available, it should be sent to VA.

(3) An appraisal must be ordered through VA. See paragraph 4.11.

(4) Upon receipt of advice that a deed is obtainable, the VARO will determine whether it is in VA's best interest to accept it. If acceptance is not approved by VA, the holder will be advised to proceed with foreclosure.

d. **Processing the Deed**

(1) If VA approves the deed, the holder and borrowers will be notified and provided further instructions. A cutoff date may be established to ensure the timely processing of the deed. If a cutoff date is established, it will usually be between 45 and 60 days after VA agrees to accept the deed. It may be extended if there are delays in obtaining the deed and related documents from the borrower(s), but extensive delay may cause VA to rescind the offer.

(2) An amount will normally be specified to be used as a credit to the indebtedness for the property. The holder will be paid the specified amount upon acceptance of the conveyance by VA. A claim will be paid for the balance of the eligible indebtedness and costs on the loan remaining after the specified amount has been credited. The following documentation is generally required to obtain payment.

(a) VA Form 26-8903, Notice of Election to Convey and/or Invoice for Transfer of Property, in triplicate, within 15 days after the deed is executed. See chapter 5.

(b) Original recorded deed from the borrower(s) to the holder and recorded deed from the holder to the Secretary of Veterans Affairs, or recorded deed from the borrower to VA.

(c) Estoppel affidavit in States where executing one eliminates or minimizes title questions. The VARO's instructions will indicate whether it is required.

(d) The executed promissory note from the obligor to VA (if required by the VARO as a condition for accepting the deed).

(e) Original mortgage documents and all recorded assignments.

(f) Title evidence in accordance with the VARO's instructions.

(g) VA Form 26-1874, Claim Under Loan Guaranty, signed by an appropriate official. See paragraph 6.02.

3.06 Refunding (38 CFR 36.4318)

a. **General**

(1) VA has discretionary authority to buy a loan in default from a holder and take over the servicing. Refunding is an optional action on the part of VA and does not provide borrowers with a right to refund their loans. Refunding is considered for each loan before

foreclosure is completed, but there is no formal application process for use by borrowers or loan holders.

(2) The objective of refunding is to avoid foreclosure when it is determined by VA that the default can be cured through various relief measures and the holder is unable or unwilling to grant further relief.

b. **Procedure**

(1) **Information Needed.** When VA believes refunding might be in order, it will notify the holder and request that it:

(a) Send VA a statement of account (VA Form Letter 26-567).

(b) Order an appraisal of the property, if one has not already been ordered. See paragraph 4.11.

(2) **Notification.** If VA decides to refund a loan, the holder will be immediately notified and given further instructions. A notice will also be sent to the borrower.

(3) **Settlement.** VA will set the date of settlement, which generally will not exceed 60 days from the date of VA's formal notice of intent to refund. The VARO of jurisdiction will provide instructions to obtain payment on the loan. Generally the following documents will be required:

(a) VA Form 26-1874 signed by an appropriate official. In item 4, Date of Loan Termination, enter the settlement date and indicate that the loan is to be refunded. See paragraph 6.02.

(b) Certified copy of the loan ledger or history.

(c) Unrecorded assignment of mortgage.

(d) Original note, endorsed to the Secretary of Veterans Affairs.

(e) Hazard insurance policy with a copy of the endorsement request.

(f) Original mortgagee's title policy, naming the Secretary of Veterans Affairs as a co-insured.

(g) Original survey of the property.

(h) Current tax receipts.

(i) Other documents specifically required in instructions issued by the VARO.

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CHAPTER 4. TERMINATION BY FORECLOSURE

4.01 Preforeclosure Analysis

a. A decision to foreclose must be based on an analysis of the individual loan with full knowledge of the alternatives and consequences to all parties to the loan. Foreclosure should not be automatic. The purpose of the preforeclosure analysis is to gain a thorough understanding of the nature and reasons for the default and the prospects for curing it, and to determine what action might avoid foreclosure.

b. The analysis should include a careful search for alternatives, including the determination whether some other party might act to avoid foreclosure. The possibilities include relatives, co-makers, Government welfare agencies, secondary lien holders, previous owners not released from personal liability, or the borrower's employer.

c. A preforeclosure review should be carefully documented. Holders should be sure the following was done:

(1) VA regulations pertaining to accepting partial payments were followed.

(2) A face-to-face interview was conducted or meaningful telephone contact made. Only with adequate information about the borrower can a proper foreclosure decision be made. If no contact was made, the efforts to contact the borrower should be well documented.

(3) VA servicing and reporting requirements were satisfied.

(4) Relief measures were considered and offered as applicable.

(5) Notice of a transferee owner's default was sent to the original veteran-borrower's last known address.

4.02 Foreclosure Recommendation

The recommendation of foreclosure should be made by the loan counselor handling the account, and be carefully reviewed by supervisory or management personnel.

4.03 Cutoff Date-Application of 38 CFR 36.4319(f)

a. **Minimizing the Loss to the Government.** VA encourages holders to extend every reasonable indulgence to worthy borrowers who are in temporary difficulty. However, when it is evident that the default is insoluble, every effort should be made to see that the security is liquidated promptly to minimize the loss to the Government.

b. **An Insoluble Default.** VA will consider any loan with 6 or more installments due and unpaid to be an insoluble default unless the holder has informed VA that a repayment plan is in effect or that forbearance is being granted for some other reason. VA may also learn through its supplemental servicing efforts that the borrower cannot or will not be able to cure the default in the foreseeable future.

c. **Establishment of a Cutoff Date**

(1) Once VA determines that a defaulted loan is insoluble, it will protect its interest by establishing a cutoff date for the computation of a claim under the guaranty, as provided by 38 CFR 36.4319(f). A claim paid under Loan Guaranty will exclude interest and most charges, other than liquidation costs, which accrue or are incurred after the cutoff date. The holder will be advised by registered mail of the establishment of a cutoff date.

(2) The cutoff date will be the date liquidation should be completed if the holder initiates appropriate action within 30 days of the date of the cutoff letter. VA considers referral to counsel to initiate public legal action to terminate the loan to be appropriate legal action for purposes of establishing a cutoff date. If a bankruptcy court has stayed the termination, appropriate action is referral to counsel to obtain relief from the automatic stay, to be followed by prompt legal action to terminate the loan. In bankruptcy cases, the cutoff date will include additional time for the holder to have the stay removed; the amount of time allowed will vary between VA offices based on their experience with the local bankruptcy courts, but generally will be 3 months after the filing date for Chapter 7 cases and 5 months for Chapter 13 cases in which no payments are received from the borrower or the trustee.

(3) A cutoff date will also be established if the holder initiates termination action timely but fails to prosecute the action with reasonable diligence. It will be based on the time normally required to complete termination from the date the initial referral to counsel was made by the holder.

(4) Appendix E contains the cutoff timeframes used by VA regional offices as of the date of publication of this handbook. These timeframes cover the period from referral to counsel until foreclosure is completed through either the sale or confirmation of sale, depending on the jurisdiction. They are for routine, uncontested, foreclosures. VA regional offices may change these timeframes based on changes in local foreclosure procedures or practices.

d. **Adjustment of a Cutoff Date.** The cutoff date can be adjusted if the holder shows that further forbearance was justified or that delay in liquidation was beyond its control. Errors or delays by the holder's counsel are considered to be within the holder's control since counsel acts as the agent of the holder. The cutoff date will be automatically adjusted if any payments are received and accepted by the holder after the cutoff date was established. Holders may request reconsideration and adjustment of a cutoff date at any time prior to payment of a claim by VA. However, once a cutoff date has been established, VA will usually review and (if appropriate) adjust it only at the time bidding

instructions are prepared or at the time the claim is being paid. The current cutoff date will be shown on any specified amount letter issued by VA.

4.04 Guaranty Computation and Cutoff Dates-Application of 38 CFR 36.4321

a. **General**

(1) This regulation has two primary purposes. The first is to define the maximum amount payable under VA's guaranty. The second is to prevent cases in which VA is unable to specify an amount solely because the loan indebtedness increased during a period of undue delay in loan termination caused by VA or the borrower.

(2) For each GI loan, the Loan Guaranty Certificate states both a percentage and a dollar amount of guaranty. The dollar amount of guaranty is equal to the percentage of guaranty as applied to the original loan amount. When a claim is payable, VA's maximum guaranty liability is the lesser of:

(a) The dollar amount of guaranty; or,

(b) The percentage of guaranty applied to the eligible indebtedness as of the liquidation sale date or a cutoff date established under 38 CFR 36.4319(f) or 36.4321(b), whichever is earliest.

(3) The eligible indebtedness is defined in 38 CFR 36.4301 as the unpaid principal plus accrued interest plus any advances or charges, allowable under the terms of the loan and actually incurred, which are authorized by statute and consistent with VA regulations. Late charges are excluded and funds applicable to the account, such as a positive escrow or suspense balance, are credited in the computation of the indebtedness.

(4) If a liquidation sale is delayed by more than 30 days as a result of a voluntary bankruptcy filed by the borrower, or forbearance requested by VA and granted by the holder, and:

(a) As of the revised liquidation sale date or the revised 38 CFR 36.4319(f) cutoff date (whichever is earlier) VA would be unable to specify an amount for credit to the indebtedness because the indebtedness increased during the interval; and,

(b) As of a date 30 days after the date VA determines the liquidation sale would have taken place, if there had been no delay due to bankruptcy or VA-requested forbearance, the unguaranteed portion of the eligible indebtedness is less than the net value of the property (i.e., VA would be required to provide the holder with a specified amount for credit to the indebtedness); then,

An adjusted cutoff date will be established under 38 CFR 36.4321(b)(1) (if the delay is due to forbearance) or 36.4321(b)(3) (if the delay is due to bankruptcy), and VA will advise the holder of the specified amount. The adjusted cutoff date will be 30 days after the date that the liquidation sale would have been held if there had been no delay.

(5) In other cases in which the liquidation sale is delayed by VA (generally those in which VA does not provide the holder with net value advice within 2 working days prior to a scheduled liquidation sale) and the delay would change a specified amount to a no-bid, VA will avoid the no-bid by using the date the sale should have been held for purposes of computing the eligible indebtedness. However, for purposes of claim computation, the actual liquidation sale date will be used. In such cases, the claim payable may not exceed the maximum guaranty plus the cost of the liquidation appraisal.

b. **Eligible Forbearance**. Generally, the terms of a repayment plan provide for liquidation of the arrears and payment of the regular monthly installment in accordance with a fixed schedule. Forbearance refers to cases in which the holder agrees to accept no payments or payments which are less than a monthly installment for a fixed period of time based on the probability that the borrower will be able to cure the default or begin a repayment plan at the end of that period. When a holder agrees to grant forbearance at VA's request, the holder should document the terms of the forbearance by letter. If the loan is not reinstated, and no amount is specified by VA in connection with a subsequent foreclosure sale, provisions of 38 CFR 36.4321(b) may be accurately applied. VA expects holders will generally provide borrowers with written notice of forbearance. A copy of this notice is adequate documentation.

c. **Effect on Claim Analysis.** Cutoff dates established as a result of bankruptcy or VA-requested forbearance will generally also apply in the computation of the holder's claim under guaranty. However, for purposes of VA's claim analysis, the account must be credited with any payments received after the cutoff date. The date of first uncured default and the cutoff date will be adjusted to account in the claim analysis. For example: Assume VA specified an amount in connection with a sale scheduled for January 1, but the sale was delayed until November 1 due to a Chapter 13 bankruptcy and, as of November 1, no amount would be specified. If an amount is specified based on the indebtedness as of January 31, VA would establish January 31 as the cutoff date and issue net value advice. If three installment payments were received under the bankruptcy, VA would credit them to the account and move the cutoff date forward to May 1 for purposes of claim computation.

4.05 Filing VA Form 26-6851, Notice of Intention to Foreclose (38 CFR 36.4317)

a. **When to File.** The holder should first exhaust all reasonable efforts to effect a cure of the default. The notice should be filed after:

(1) The loan is delinquent for 3 months (38 CFR 36.4316), and

(2) The default is determined insoluble.

In exceptional circumstances, such as a hazard to the security or material prejudice to the holder's rights or to VA, the notice may be filed earlier. When a loan is more than 30 days delinquent, a property abandonment must be reported to VA and liquidation action initiated within 15 days after the holder confirms the property is vacant. Referral to an attorney to begin foreclosure constitutes initiation of liquidation action.

b. **Filling Out the NOI**

(1) The NOI must be sent by registered or certified mail with return receipt requested. Figure 4-1 is an example of a properly completed NOI.

(2) In filling out the NOI, holders should pay special attention to the following:

(a) **VA LIN (VA Loan Identification Number)**. The VA LIN must be numeric and 12 digits in length. See appendix B for instructions.

(b) **Holder's Name, Address, and Telephone Number (Item 1A)**. Provide a telephone number so VA loan service representatives can contact the holder's personnel directly.

(c) **Original Veteran's Name and Present Address (Item 2)**. If someone other than the original veteran is the present owner, the name and current address of the original veteran should be provided. For purposes of the NOI, the original veteran's name is required by 38 CFR 36.4332. His or her current address should be the most recent available in the holder's system of records. (After a notice of intention to foreclose is filed, holders must make an effort to determine the original veteran's current address (see par. 4.07)). Because veterans may be held liable to reimburse the Government for claims paid due to transferee defaults, VA requires this information to try to provide veterans with notice of transferee defaults. In some areas, generally those in which foreclosure cannot be completed quickly, it is not essential that VA have this information at the time the NOI is filed. Since many holders do not retain data on prior obligors in their automated servicing records, each VA office of jurisdiction has issued a release informing holders whether or not they must strictly adhere to this regulatory requirement.

(d) **Other Transferee Data (Item 7)**. If item 6 is checked "yes," provide the names of those who held title to the property other than the original veteran and the current property owner. If the transferee's address, name of employer and address of employer are not on record, type "unknown" in the appropriate blocks.

(e) **Voluntary Conveyance Data (Item 11)**. Holders often neglect to check the appropriate block to indicate whether or not a voluntary conveyance is obtainable. Usually, through personal contact, the holder can determine whether there are any

secondary liens which encumber the property that would preclude a voluntary conveyance. Check whether such a deed is feasible.

(f) **Holder's Loan Servicing (Item 12)**. It is important that VA have complete information about the reasons for the default and decision to foreclose. This space also provides the holder with the opportunity to document the quality of its servicing by showing that it has discussed alternatives to foreclosure with the borrower and to indicate the borrower's responsiveness. Use the back of the NOI or a separate sheet of paper if more space is needed. A narrative summary of any contacts made with the borrower since filing the NOD is also useful. If no contact was made, give a history of the attempts made. What alternatives to foreclosure were suggested? Which appear feasible? Why are some not feasible? A copy of the in-house servicing record is acceptable as long as the VARO has been provided with instructions on how to read it and explanations of any abbreviations it contains.

(g) **Occupancy Data (Item 13)**. Report who is occupying the property, or if it is vacant, where the keys may be obtained and whether the property has been secured.

(h) **Signature (Item 15)**. The form must be signed by a corporate officer or other authorized full-time employee of the holder or its servicing agent. If the proper signature is omitted, the form will be returned.

4.06 Filing VA Form 26-6850a, Notice of Default and Intention to Foreclose (38 CFR 36.4317)

a. **When to Use the NOD&I.** The NOD&I allows the holder to simultaneously notify VA that a loan is in default, the default is insoluble, and that it intends to proceed with foreclosure. This form may be used if:

(1) The property is abandoned.

(2) It is determined that the loan is insoluble before the NOD is filed.

(3) Delay in termination action may expose the security to waste or hazard or may cause material prejudice to the rights of the holder or VA.

b. **Waiver Request.** If appropriate, the holder should request a waiver of the 30-day waiting period before initiation of legal action (38 CFR 36.4317).

c. **Completing and Sending the NOD&I.** The NOD&I must be sent by registered or certified mail with return receipt requested. Figure 4-2 contains an example of a properly completed NOD&I. In filling out the NOD&I, holders should pay special attention to the following:

(1) **VA LIN (VA Loan Identification Number) (Item 3)**. The VA LIN must be numeric and 12 digits long. See appendix B for instructions on constructing the VA LIN.

(2) **Holder's and Servicing Agent's Phone Number (Item 6)**. Provide a telephone number so VA loan service representatives can contact the holder's personnel directly.

(3) **Date of First Uncured Default (Item 9)**. This is the due date of the first or earliest partially or fully unpaid installment.

(4) **Present Owner's Social Security Number (Item 10)**

(5) **Original Veteran's Name and Present Address (Item 16)**. If the default occurs when someone other than the original veteran is the present owner, the name and current address of the original veteran should be provided. See paragraph 4.05b(2)(b).

(6) **Occupancy Data (Item 20)**. Report who is occupying the property, or if it is vacant, where the keys may be obtained and whether the property has been secured.

(7) **Other Transferee Data (Item 21)**. Provide the names of anyone who held title to the property after the original veteran and before the current property owner. If the transferee's address, name of employer and address of employer are not on record, type "unknown" in the appropriate blocks.

(8) **Voluntary Conveyance Data (Item 23)**. Holders often neglect to check the appropriate block to indicate whether or not a voluntary conveyance is obtainable. Usually through personal contact the holder can determine whether there are any secondary liens which encumber the property that would preclude a voluntary conveyance. Check whether a deed is feasible.

(9) **Present Owner's Telephone Number (Items 27E and 27F)**. A diligent effort should be made to obtain the telephone number of both the property owner's place of employment and home. If a number is not available, note in the servicing summary what efforts have been made to obtain the number. This will prevent the duplication of effort when VA begins supplemental servicing.

(10) **Reason for Default and Summary of Loan Servicing (Item 28)**. It is important that VA have complete information about the default and the prospects for resolution. Use the back of the NOD&I or separate sheet of paper if more space is needed. Provide a summary of contacts made with the borrowers or the attempts made if there was no contact and the reasons for filing a combined NOD and NOI. A copy of the in-house servicing record is acceptable as long as the VA regional office has been provided with instructions on how to read it and explanations of any abbreviations it contains.

(11) **Signature (Item 30)**. The form must be signed by a corporate officer or other authorized full-time employee of the holder or its servicing agent. If the proper signature

is omitted, the form will be returned. The individual signing the notice should review the form to see that the information provided is accurate.

4.07 Notice to Original Veteran-Borrower and Other Liable Obligors

(38 CFR 36.4317)

a. A notice of intention to foreclose must also be sent to the original veteran-borrower, if still a liable obligor, and any other liable obligors when the current owner of the property is not the original veteran-borrower. The notice must be sent by registered mail within 30 days after such notice is provided to VA. A failure by the holder to make a good faith effort to comply with these requirements may result in a partial or total loss of guaranty. A good faith effort will include, but is not limited to:

(1) A search of the holder's automated and physical loan record systems to identify the name and current or last known address of the original veteran and any other liable obligors;

(2) A search of the holder's automated and physical loan record systems to identify sufficient information (e.g., Social Security Number) to perform a routine trace inquiry through a major consumer credit bureau;

(3) Conducting the trace inquiry using an in-house credit reporting terminal;

(4) Obtaining the results of the inquiry;

(5) Mailing the required notices and concurrently providing VA with the names and addresses of all obligors who have been identified and notified; and,

(6) Documentation of the holder's records.

b. VA will reimburse the holder $10 in its claim under guaranty, as a liquidation expense, for each obligor subject to this procedure.

4.08 Starting Liquidation Proceedings

a. **30 Day Delay Before Starting Foreclosure** (38 CFR 36.4317)

(1) The NOI or NOD&I must be filed at least 30 days prior to starting any action to liquidate the security for the loan. Failure to give proper notice of foreclosure may result in an adjustment in the amount of the claim payable if it increased VA's liability.

(2) If the circumstances warrant immediate action to protect the interest of the holder and VA (such as abandonment of property), the holder may take action without advance notice. In such instances the holder must promptly notify VA of the action taken. Except in cases of abandonment, VA would prefer that when warranted, the holder file a NOI or

NOD&I in advance of initiating foreclosure action and request waiver of the 30-day waiting period. If waiver is warranted, VA will immediately respond by giving approval to begin foreclosure action.

b. **Election of Liquidation Procedure.** (38 CFR 36.4324(f)) VA will notify the holder within 15 days of receipt of the NOI if it requires the holder to act to preserve the personal liabilities of the obligors. Otherwise, the holder may elect any available liquidation procedure.

c. **Persons in Possession of Property.** The holder should make persons in possession under a claim of title parties to any judicial foreclosure proceedings and cause them to be properly served. In nonjudicial foreclosure the holder should take any feasible legal steps available under local law, by notice or otherwise, to prevent the rights of any such persons from surviving the foreclosure to ensure VA will be provided with acceptable title after foreclosure.

4.09 Other Notices to VA (38 CFR 36.4319)

Holders must notify the appropriate VARO of any steps contemplated or action taken in connection with the liquidation of the security. A copy of every procedural paper filed on behalf of the holder and of each pleading served on the holder must be sent to VA.

4.10 Reinstatement of Defaulted Loans (38 CFR 36.4308(h))

a. **Acceptance of Funds.** If sufficient funds are tendered to bring a defaulted loan current at any time prior to a sale to liquidate the security for a guaranteed loan, the holder must accept the funds in payment of the delinquency unless:

(1) The prior approval of VA is obtained to do otherwise, or

(2) Reinstatement of the loan would adversely affect the dignity of the lien or is otherwise precluded by law.

b. **Definition of the Delinquency.** The delinquency will include:

(1) All installment payments (principal, interest, taxes, insurance, advances, etc.) due and unpaid.

(2) Any accumulated late charges.

(3) Any reasonable expenses incurred and paid by the holder if termination proceedings have begun (e.g., advertising costs, foreclosure costs, attorney or trustee fees, recording fees, appraisal costs).

4.11 Liquidation Appraisal

a. **Ordering the Appraisal.** At least 30 days before the foreclosure sale date (sooner, if the VARO has issued instructions requiring or permitting it to be ordered earlier), the holder must request from the appropriate VARO the assignment of an appraiser to determine the fair market value of the security. Holders should fill out VA Form 26-1805, VA Request for Determination of Reasonable Value/HUD Application for Property Appraisal and Commitment, and forward all copies except 1 and 2 to the assigned appraiser.

b. **Assisting the Appraiser.** Holders must assist the appraiser in gaining interior access to the property unless prohibited by local law. If the property is occupied, the appraisal request must include the name and number of current or last known occupants. If the property is vacant, keys should be given to the appraiser or other arrangements made for access. If the holder fails to assist the appraiser to obtain access and the foreclosure sale has to be postponed, 38 CFR 36.4319(f) may be invoked and a cutoff date established to limit the liability of VA.

c. **The Appraisal Fee.** The holder will pay the appraisal fee, which may be included as a liquidation cost in the claim. Each VARO sets the amount of the liquidation appraisal fee for its jurisdiction. After the appraisal has been ordered, the fee should be included in the amount of the delinquency if the borrower wishes to bring the loan current.

4.12 Notice of Sale (38 CFR 36.4319(b))

A copy of a notice of liquidation sale must be delivered to VA at least 30 days prior to the scheduled foreclosure sale or within 5 days of the first publication date, whichever is later. The notice must be accompanied by a copy of the liquidation appraisal request, VA Form 26-1805 and a statement of account, VA Form Letter 26-567, if these documents have not previously been delivered. See figure 4-3 for an example of a properly completed VA FL 26-567, Status of Loan Account - Foreclosure or Other Liquidation.

4.13 Bidding Instructions (38 CFR 36.4320)

a. **General.** A foreclosure sale should not be held unless the holder has received instructions from VA. Normally, a letter of instruction will be sent in time to be received by the holder at least two working days prior to the date of the scheduled foreclosure sale. When time does not permit mailing instructions, VA will give instructions by telephone or electronic media, and confirm by letter. If the holder does not receive notification, it should contact the VARO in advance of the scheduled foreclosure sale.

b. **Total Indebtedness**

(1) When the net value of the loan security exceeds the total indebtedness (debt plus costs), the holder will be instructed by VA Form Letter 26-639, Specified Amount Letter (fig. 4-4) that the credit to the indebtedness on account of the sale must be the total indebtedness.

(2) When total indebtedness is specified, the holder should calculate the indebtedness to the foreclosure sale date or the cutoff date established under 38 CFR 36.4319(f), including allowable foreclosure costs and expenses (see par. 4.17), and bid that amount at the sale. When instructions are received verbally, the holder should make certain they are accompanied by any revision to the cutoff date. There will be no claim payable by VA when total indebtedness is specified and the property is bought by a third party or retained by the holder. If the property is conveyed to VA, the unpaid principal balance will be paid for transfer of the property. A final accounting with VA after title is accepted, using VA Form 26-1874, Claim Under Loan Guaranty, must be received and analyzed before the balance of the indebtedness is paid.

c. **VA Specified Amount**

(1) When the net value of the loan security is greater than the unguaranteed portion of the indebtedness but is less than the total indebtedness, VA will advise the holder to credit to the indebtedness on account of the sale a specific dollar amount. This amount will be equal to the net value of the security to VA.

(2) If an amount is specified, advice to the holder will be given by VA Form Letter 26-639 (fig. 4-5). The holder should not bid more than the specified amount at the foreclosure sale unless the holder desires to keep the property. If the holder bids in excess of the specified amount, the accounting with VA will be based on the bid, and the holder will not have the option of conveying the property to VA (see par. 4.14). If the holder allows a third party to acquire the property with a bid of less than the specified amount, it will lose the difference between the successful third party bid and the specified amount.

d. **No Specified Amounts (No-Bids)**

(1) When the net value of the loan security is less than the unguaranteed portion of the indebtedness, VA will not specify an amount for the holder to credit to the indebtedness on account of the sale and will not accept conveyance of the property.

(2) If no amount is specified by VA, a bid in excess of the indebtedness (including allowable foreclosure expenses) less the amount payable under the guaranty may reduce the amount of claim payable by VA. The net value of the property is stated by VA in the no-bid advice letter. Holders should be cautious about bidding in excess of the net value, unless they wish to ensure they acquire the property, because such a bid may exceed the unguaranteed portion of the indebtedness and reduce the amount of claim payable by VA.

e. **Partial Waiver of Indebtedness to Obtain a Specified Bid (No-Bid Buydown)**

(1) **Procedure**

(a) Upon receipt of advice that no amount will be specified for credit to the indebtedness, the holder may waive or satisfy a portion of the indebtedness to reduce it to an amount which would require VA to provide a specified amount and acquire property under 38 CFR 36.4320. The waiver may take the form of a reduction of the principal balance, credit to escrow or the unapplied funds account, forgiveness of unpaid accrued interest or a combination of these credits.

(b) VA has two legal concerns about partial debt waivers or reductions. The holder's action must not affect the validity of the foreclosure or the validity of the indebtedness which may be established against the obligors and must be binding on all parties to the loan agreement and documented by appropriate entries to the account ledgers. It cannot be rescinded without the approval of all parties to the loan agreement. Subject to these concerns, VAROs will determine the debt reduction procedure(s) acceptable in their jurisdiction and will make this information available upon request.

(2) **Adjustment of Cutoff Dates.** VA regulations require that the indebtedness as of the cutoff date be used for determining VA's guaranty liability and for determining whether or not an amount will be specified for credit to the indebtedness on account of a foreclosure sale. There will be occasions when the holder is not advised that no amount will be specified until after a cutoff date has passed. In such cases, the holder would be effectively denied the opportunity to reduce the indebtedness to obtain a specified amount from VA. To give the holder the opportunity to reduce the indebtedness, any advice to a holder that no amount will be specified by VA will be accompanied by a statement to the effect that the existing cutoff date will be rescinded and replaced by a revised cutoff date, which will be 30 days from the date of the advice. Consideration will be given to extending the 30 day limit to 60 days when holders advise VA that additional time is necessary for them to secure required approvals for debt reduction or when local law does not permit rescheduling the sale within 30 days.

4.14 Overbids at Foreclosure Sales (38 CFR 36.4320(a)(1)(ii)(B))

a. If an amount was specified, and the holder acquires the property at the liquidation sale for an amount in excess of the specified amount, the indebtedness must be credited with the proceeds of the sale. The holder will not have the option to convey the property to VA.

b. In some States, the holder can legally amend the amount bid at a sale or set aside or vacate the sale. Holders should consult with the appropriate VARO and their own counsel regarding possible methods to correct an overbid. Notice of all legal actions must be provided to VA (38 CFR 36.4319(a)).

c. If a new sale is scheduled, the date of the first sale will be the cutoff date for the purposes of claim computation. The procedures for providing notice of sale (par. 4.12) and ordering a liquidation appraisal (par. 4.11) should be followed so that appropriate advice can be provided by VAROs in a timely manner.

4.15 Property Preservation

a. A holder is responsible for measures needed to protect and preserve the security for the loan, especially when the property becomes vacant. This responsibility ends when VA accepts custody of the property after receiving the holder's VA Form 26-8903, Notice of Election to Convey and/or Invoice for Transfer of Property.

b. The property must be inspected at least once a month after liquidation proceedings have been started, unless servicing information shows the property has remained owner-occupied (see par. 2.04, Property Inspections). VARO releases describe the measures to be taken in securing vacant properties and the maximum expenses allowed.

c. VA must be notified of any damage to the property or if it is abandoned, especially after the bidding instructions have been sent. (38 CFR 36.4320(e))

4.16 Deficiency Judgment

Unless a personal deficiency judgment is routinely obtained incident to the foreclosure, VA requires the holder to obtain one only when it is necessary to preserve the personal liability of the obligors and VA has requested the holder to do so upon receiving the notice of intention to foreclose. In such cases, VA will allow the cost of obtaining a deficiency judgment to be included in the claim. In other cases, the holder may also obtain a deficiency judgment at its own expense to protect its interests provided foreclosure is not delayed.

4.17 Acceptable Expenses (38 CFR 36.4313(b))

a. The following expenses may be included in any accounting with VA, and in the computation of a claim under the guaranty, if authorized by the loan agreement:

(1) Any expense reasonably necessary for preservation of the security. VARO releases list the maximum amounts that will be reimbursed for various property preservation measures in their area, including property inspections.

(2) Court costs in a foreclosure or other prior judicial proceeding involving the security.

(3) Other expenses reasonably necessary for collecting the debt or liquidation of the security, including preliminary title and tax search costs which are not considered part of

the attorney or trustee's fee and are not included in the cost of title evidence allowable under 38 CFR 36.4320(f)(2).

(4) Reasonable trustee's fees or commissions not in excess of those allowed by statute and in no event in excess of 5 percent of the unpaid indebtedness.

(5) A reasonable amount for legal services actually performed, as determined by the VA office of jurisdiction. In no event may this amount exceed 10 percent of the unpaid indebtedness as of the date of the first uncured default, or $700, whichever is less.

(6) Reasonable and customary costs of property inspections.

(7) Any other expense or fee that is approved in advance by VA.

b. The total amount of trustee's fees and legal services may not exceed $700 unless prior approval for a higher figure has been granted by the VARO. Such approval will normally only be granted for services which are uniquely necessary because a VA-guaranteed loan is the subject of the litigation. VA does not allow legal fees in connection with a bankruptcy, but will reimburse the holder up to $100 for each court appearance made by counsel in connection with the action. The number of appearances and the fees paid must be documented with the holder's claim.

c. As noted in paragraph 4.07, a charge of $10 for each prior obligor who must be provided with notice of the holder's intention to foreclose may also be included in the claim.

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CHAPTER 5. CONVEYING REAL PROPERTY TO VA

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CHAPTER 5. CONVEYING REAL PROPERTY TO VA

5.01 Background

a. Prior to the liquidation sale of a VA-guaranteed loan, holders receive advice from VA on how to proceed and whether the holder will have the opportunity to convey the property to VA. This is accomplished through the form letters described in paragraph 4.13, which are commonly referred to as either "bid (specified amount or net value) letters" or "no-bid letters." These letters require the holder to credit the account indebtedness with the specified amount for purposes of accounting with VA, even if a lesser amount is bid at the foreclosure sale. If a greater amount is bid, the account must be credited with the net proceeds of the sale.

b. If VA specifies an amount for the holder to bid at the liquidation sale or instructs the holder to bid the total indebtedness, the holder can convey the property to VA as long as the bid at the sale does not exceed the specified amount. Payment for the property will be authorized when evidence of acceptable title is approved by VA. The holder will be sent a letter at that time indicating when it should expect to receive payment. As consideration for the conveyance, VA will pay the holder:

(1) The specified amount; or,

(2) The total eligible indebtedness, if VA advised the holder to credit the total indebtedness on account of the sale. This type of bid letter is commonly referred to as a "debt plus costs" or "total debt" letter.

5.02 Custody Retained by the Holder

Holders normally convey property to VA after a loan has been liquidated. However, there are five reasons that holders retain title:

a. The holder chooses to do so;

b. VA issues "no-bid" advice which precludes the holder from conveying the property to VA;

c. A failure to follow the regulations which form the basis of VA's guaranty (e.g., notice of election to convey the property is not received by VA within 15 days after the sale, bid at the sale exceeded the net value of the property);

d. Acceptable evidence of title cannot be provided; and/or,

e. Acceptable evidence of title is not provided timely.

5.03 Condominiums (38 CFR 36.4320(h)(10))

A condominium may be conveyed to VA only if the property, including the elements of the development or project owned in common with other unit owners, is undamaged by fire, earthquake, windstorm, flooding or boiler explosion. VA may agree to accept conveyance of a damaged condominium if repairs are completed within a given period of time.

5.04 Transfer of Custody to VA

a. **VA Form 26-8903, Notice for Election to Convey and/or Invoice for Transfer of Property.** When a holder has the option to convey liquidated property to VA and chooses to do so, the holder must notify VA on VA Form 26-8903 in triplicate. An example of a completed Notice of Election to Convey appears in figure 5-1. The notice must be received not later than 15 days after the date of sale or confirmation of sale. To facilitate processing of the conveyance, VA generally provides a partially completed VA Form 26-8903, together with instructions as to the title documentation which will be required, along with the specified amount letter.

b. **Acceptance of Custody.** VA will accept custody of the property upon receipt of this form unless the holder specifically requests to retain custody until conveyance of the property is approved. If VA has not processed receipt of VA Form 26-8903, the holder will be mailed VA Form 26-8802, Request to Lender for Results of Foreclosure - LCS, which requests the results of the foreclosure sale, 30 days after the scheduled sale date. The holder should immediately check its records to verify that custody has been transferred to VA and contact the VA office of jurisdiction to confirm whether or not the notice has been received. Conveyance will not be accepted until the title package is reviewed and approved. Upon acceptance of the holder's conveyance or transfer, VA will pay the consideration for the property.

c. **Risk of Loss.** (38 CFR 36.4320(h)(10)) The holder remains responsible for loss due to property damage or personal injury at the property from the date it acquires the property until risk of loss is assumed by VA. Assumption of the risk of loss by VA usually occurs when VA receives the holder's VA Form 26-8903 and accepts custody. At this time the holder should discontinue all property management functions unless it is retaining custody.

5.05 Title

a. **Designation of Grantee.** Conveyances to VA should be made out to the "Secretary of Veterans Affairs, an Officer of the United States of America, successors and assigns, at (VA office of jurisdiction address)." This language may be modified so long as the form of the modification is legally acceptable in the area. Care must be taken to ensure the office of jurisdiction's address is used.

b. **Conveyance by General Warranty.** (38 CFR 36.4320(h)(5)(ii)) In most areas, a supervised lender or a holder of financial responsibility satisfactory to VA may convey property to VA with a general warranty deed instead of providing evidence of acceptable title. When a general warranty is tendered (either in the conveyance or by separate instrument), the conveyance will be accepted and placed on record immediately and title examination will not be required. The holder must still deliver to VA the title evidence it has.

c. **Conveyance with Special Warranty and Acceptable Title Evidence**

(1) **Special Warranty.** When a general warranty is not used, the conveyance will be with "special warranty" only. The grantor covenants (or "warrants") in the deed or by separately executed instrument against any claim to the property, or any interest therein, adverse to grantee (Secretary of VA) by such grantor (transferor) and by any person or persons claiming through or under it.

(2) **Acceptable Title Evidence** (38 CFR 36.4320(h)(5))

(a) Title to any real property conveyed to VA must be of the same quality as the title generally required by prudent lenders, informed buyers, title companies, and attorneys in the community where the property is located. The definition of acceptable title evidence may vary from State to State. Each VARO has issued a release describing the title evidence and documents required in its jurisdiction. Holders should receive a copy of these instructions with the bid letter when the holder has an opportunity to convey the property to VA.

(b) In most areas of the country, loan holders may submit title policies as acceptable title evidence and transfer deeds when transferring title of property to VA. VA encourages use of this procedure whenever it will facilitate the title approval process.

(3) **Cost of Title Evidence.** The customary cost of title evidence will be borne by VA. The costs may not exceed the rates charged generally by local title companies. In certain areas VA may save time and expense by making arrangements with title insurers or others for furnishing title policies or other evidence of title. Holders will be notified of the arrangements and should use such sources to obtain the required title evidence. If the VA office of jurisdiction has negotiated a reduced fee for title evidence from one or more specific companies, holders will only be reimbursed at the negotiated rate unless a persuasive argument can be made for the need to obtain higher cost evidence.

(4) **Quality of Title** (38 CFR 36.4320(h)(5))

(a) Encroachments, easements, restrictions with or without condition of reverter, and other matters enumerated in the regulations (38 CFR 36.4350(b)) will not constitute objections to the acceptance of title. However, if these items were not taken into account in determining the reasonable value at loan origination, an adjustment of the claim may be made.

(b) When the property is to be conveyed, there must not have been a breach of any of the conditions affording the right to the exercise of any reverter. However, title will not be unacceptable to VA by reason of a violation of a restriction based on race, color, religion, sex or national origin, even if the restriction provides for revision or forfeiture of title or a lien for liquidated damages in the event of a breach.

(c) The holder should have made persons in possession under a claim of title parties to any judicial foreclosure proceedings and caused them to be properly served. The final decree should appropriately dispose of the rights of such parties. In nonjudicial foreclosure the holder should have taken any feasible legal steps available under local law, by notice or otherwise, to cut off the rights of any such persons.

d. **Timeliness**

(1) Holders should submit title packages to VA as early as possible because delays are costly to both VA and holders. Holders are not compensated for interest accruals after completion of liquidation.

(2) The time allowed will generally be 60 days from the date of sale or confirmation of sale, whichever is applicable. Each VARO has issued informational releases regarding timeliness and includes this information in the title submission instructions sent with the bid letter. VARO instructions which allow more than 60 days take precedence over the general 60 day rule.

(3) A holder that encounters an unavoidable delay in gathering the necessary title evidence should request an extension before the end of the time limit set by the VARO. The holder should send VA a written explanation of the cause of the delay.

(4) Failure to timely submit a complete title package or an acceptable request for an extension may result in reconveyance of the property.

e. **Title Objections**

(1) When title is found to be unacceptable, the holder may be given a reasonable period of time to correct the objections depending on the circumstances of the particular case. An extension is a matter of discretion and not a legal right. A written stipulation, stating the duration and the conditions of the extension, must be signed by the holder and by VA.

(2) When more than 30 days will be required to cure the title problem, the holder will generally be required to retain or resume custody of the property and to assume responsibility for all carrying charges, such as taxes and maintenance, and any decrease in the value of the property, from the date stated in the stipulation granting the extension until the title is acceptable to VA.

(3) If title objections cannot be cleared within a reasonable time, the holder will be required to retain the property and credit the indebtedness with the specified amount. VA may, at its discretion, agree with the holder to accept title with an adjustment of the amount that would otherwise be payable, based upon the diminution in the value of the property because of the title defects.

f. **Subsequently Discovered Title Defects.** (38 CFR 36.4320(h)(6)) VA's legal rights are limited in certain respects as to title defects discovered after delivery of a conveyance has been accepted. Generally, once VA has accepted title, the holder is not responsible for clearing defects which are subsequently discovered unless they are covered under covenants or warranties given VA by the holder in conveying the property.

5.06 Property Preservation

a. During the time between the foreclosure sale date or confirmation of sale date, and the date of receipt by VA of the holder's notice of election to convey the property, holders should perform emergency property preservation repairs not in excess of $500. Repairs in excess of $500 must be approved in advance by VA. This limitation does not apply to expenditures for heat, water, electricity, or other services where:

(1) Properties are occupied by tenants,

(2) The terms of the rental agreements require the landlord to furnish such services; and

(3) Upon acquisition of the property by the holder the tenants are obligated to pay rents to the holder.

b. VA will generally assume these functions when custody of the property is transferred.

5.07 Rentals

a. The holder may not rent the property to a new tenant or extend an existing tenancy on other than a month-to-month basis unless the prior approval of VA is obtained. (38 CFR 36.4320(h)(3))

b. When the holder has continued custody of the property, or custody has been returned to the holder by VA, the holder must, after conveyance to VA, account for all

rents and other income collected and authorized disbursements made. (38 CFR 36.4320(h)(9)) If VA declines to accept a conveyance of the property over which it assumed custody, it will account to the holder for collections and disbursements.

5.08 Hazard Insurance (38 CFR 36.4320(h)(2))

a. The holder must not cancel any insurance in force when it acquires the property unless the VA office of jurisdiction has specifically waived this requirement and requested that the policy be canceled and a refund of the unearned premium obtained. VA may take such action in areas in which the insurance policy in force does not extend coverage to a party who acquires title through foreclosure or to that party's grantee.

b. After a property has been conveyed to VA, the holder must deliver to VA, properly endorsed, all hazard insurance policies in force which had been obtained before the holder acquired the property. Policies are to be endorsed so that any amounts payable by the insurer will be paid to VA. The endorsement should be made out to "Secretary of Veterans Affairs, an Officer of the United States of America, at (VA office of jurisdiction address)."

5.09 Taxes (38 CFR 36.4320(h)(4))

The holder must pay any taxes, special assessments, or ground rents due and payable within 30 days after the date of conveyance if the bills are obtainable.

5.10 Acceptable Conveyance Expenses (38 CFR 36.4320(f))

The following expenses may be included in any accounting with VA in the computation of a claim under the guaranty, if paid by the holder:

a. Required State and documentary stamp taxes.

b. The customary cost of obtaining evidence of title, as discussed in paragraph 5.05c(3). The costs of title evidence obtained incident to making the loan or any expenses incurred to clear title defects may not be included.

c. Taxes, special assessments, or ground rents, as discussed in paragraph 5.09.

d. Recording fees.

e. Any other expenditures connected with the property approved in advance by VA.

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CHAPTER 6. CLAIMS PROCEDURES

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CHAPTER 6. CLAIMS PROCEDURES

6.01 General

a. Holders may submit claims under the guaranty after a loan has been terminated by foreclosure or the acceptance of a voluntary conveyance (deed in lieu of foreclosure). A claim must also be submitted if VA elects to purchase, or refund, the loan. In that case, the instructions in paragraph 3.06, Refunding, should be followed. Procedures are also different in a compromise agreement (see par. 3.04).

b. A claim should generally be submitted after all expenses involved with a terminated loan have been paid. VA will accept a supplemental claim at a later date should an item be omitted from the original claim, but as a practical matter, holders should try to include all expenses in the original claim because processing primary claims is given priority over supplementals.

c. For timely payment, it is in the holder's best interest to ensure that the claim form and supporting documents are complete and meet VA requirements.

6.02 VA Form 26-1874, Claim Under Loan Guaranty

This form should be submitted in duplicate along with appropriate supporting documents. The original must be signed by a corporate officer or other full-time employee of the holder authorized to execute claims. A completed example of this form appears in figure 6-1. In completing this form, holders should pay special attention to the following items:

a. Claimant (item 1) and holder's loan number (item 3B) when FNMA is the holder. Be sure to list FNMA as the claimant and give the FNMA number as the holder's loan number.

b. **Payments**. This involves principal and interest only, not tax and insurance amounts. Item 5B should total items 5C and 5D. Interest in item 5C must include any interest adjustment shown on the HUD-1 form or VA Form 26-1820, Report and Certification of Loan Disbursement.

c. **Principal Balance (Item 11A)**. This is the unpaid principal balance of the loan after credit is given for all payments received from the borrower.

d. **Balance in T&I Account (Item 11C)**. If any advance was made for the payment of taxes or an insurance premium, the balance should be zero.

e. **Miscellaneous Credits (Item 11G)**. Provide a breakdown and explanation of the amounts involved. Attach a separate sheet if necessary.

f. **Itemized Advances (Item 12)**. If the T&I account balance was not sufficient to pay taxes or insurance when due, only the deficiency (shortage) should be shown as an advance. Late charges or tax penalties must not be included. Care should be taken to itemize advances prior to and after a cutoff date. Because many advances are subject to caps established by the VA office of jurisdiction, such as property preservation charges and some liquidation costs, holders should obtain current releases on allowable fees from each VA office with which they may be filing a claim and limit the amount claimed for advances to the amount allowable.

6.03 Other Required Documents

The following documents are required when submitting a claim:

a. Originals or certified copies of all instruments evidencing the indebtedness and the agreement between the claimant and the debtor. Copies of instruments which have been recorded must show book, page, date, and place of recording. The note or evidence of the debt should be endorsed as follows (except where the holder will not be made whole and plans to pursue collection from the obligor) :

Pay to the order of the Secretary of Veterans Affairs, without recourse.

_____
(Holder)

_____
(Official Signature)

_____
(Title)

The note or other instrument should not be marked "paid" or "canceled."

b. If claimant is an assignee or transferee of the original lender, a certified copy of the instrument of transfer.

c. If a judgment has been obtained, an assignment thereof (in addition to the note, unless by law or order of the court it is retained among the court papers) to the Secretary of Veterans Affairs with advice of the amount, if any, collected on the judgment.

d. Certification that the loan termination has been reported to the credit bureaus.

e. A certified statement of account. This in effect should be a copy of the ledger sheets or equivalent showing the amounts and dates of all debits and credits to the account.

f. Copies of all deeds transferring title from the original veteran-obligor through the owner holding title at liquidation. Social Security or taxpayer identification numbers of transferees should be annotated on the deeds.

g. Copies of all judicial proceedings involving the foreclosure and any bankruptcies, if not previously provided to VA.

6.04 Computation of Claim

a. Ordinarily, a proper claim will be processed within 30 days of receipt if it is in good order and accompanied by the required documents. VA will determine whether the claim is eligible for payment under the guaranty. All claims will be checked for accuracy, the propriety of the charges, and to verify proper disposition of funds.

b. The total amount claimed (item 11H on VA Form 26-1874) does not include interest. VA will calculate the accrued interest from the date of the last paid installment to one of the following dates, whichever is applicable:

(1) The date of liquidation;

(2) The date the deed is recorded (in a voluntary conveyance); or,

(3) A cutoff date established under the provisions of 38 CFR 36.4319(f) or 38 CFR 36.4321(b).

c. For purposes of determining VA's guaranty liability, the total indebtedness as calculated by VA will include unpaid principal, accrued interest to the cutoff date, advances, and liquidation and property preservation expenses if paid prior to the cutoff date and allowable by regulation. Advances and liquidation expenses paid after the cutoff date may be included in the holder's claim and are reimbursable to the extent that the total claim payable does not exceed VA's guaranty liability. Advances for insurance paid after the cutoff date, however, may not be included in the claim. Advances for real estate taxes, assessments, or ground rents paid after the cutoff date are generally fully reimbursable unless a cutoff date which is prior to the liquidation sale date has been established under 38 CFR 36.4319(f), 36.4321(b)(1) or 36.4321(b)(3). If an earlier cutoff date is in effect, these costs may be allowed only on a pro rata basis through the cutoff date. However, advances for taxes which must be paid pursuant to paragraph 5.09 (38 CFR 36.4320(h)(4)) are reimbursable on the same basis as liquidation expenses paid after the cutoff date.

d. VA will also reimburse holders for the cost of the liquidation appraisal, and advances and expenses which were requested to be paid by the holder on behalf of VA. For example, as a result of the timing of a foreclosure sale, property taxes are due more than 30 days after the liquidation sale but there is insufficient time for VA to accept custody of the property and pay the taxes so that a penalty will be avoided. In such a situation, VA might authorize the holder to pay the tax and then reimburse the holder even if payment exceeds the maximum claim payable. Similarly, if a holder obtained VA's prior approval to make emergency repairs to the property, then expenses are reimbursed to the holder.

e. Items or amounts claimed that are not eligible, in excess of the allowable amount, not supported by paid receipt, or not itemized, will be disallowed.

6.05 Limit to Claim

The amount paid cannot exceed the amount or percentage guaranteed. The guaranty increases or decreases pro rata with any increase or decrease in the amount of guaranteed indebtedness up to the amount originally guaranteed. For example, if VA originally issued a $36,000, 40 percent guaranty on a $90,000 loan and the indebtedness at liquidation was $95,000, then the guaranty is capped at $36,000. If indebtedness at liquidation on the same $90,000 loan was $80,000, the amount of guaranty would be 40 percent or $32,000.

6.06 Partial or Total Loss of Guaranty (38 CFR 36.4325) and Suspension (38 CFR 36.4332)

a. **Forgery.** Forgery of the security instruments, loan or guaranty application or other loan processing documents which are essential to the underwriting process releases VA from guaranty liability on the loan, regardless of the current holder. A counterfeit or falsified discharge certificate or certificate of eligibility is similarly treated.

b. **Fraud or Willful Misrepresentation**

(1) A finding that the original lender obtained guaranty of a loan as a result of willful and material fraud or misrepresentation will provide a basis for denial of liability by VA if the fraud or misrepresentation affected VA's decision to guaranty the loan. Examples of fraud and willful misrepresentation include:

(a) Hiding unacceptable credit by obtaining multiple credit reports and including only the report that shows acceptable credit history in the loan package;

(b) Materially false information in the loan package as a result of allowing the veteran to hand-carry employment, deposit or other income or credit verifications instead of mailing them directly to the employer, depository or other proper source of information;

(c) Not reporting a second lien executed in connection with the loan closing to reimburse the seller or a third party for costs of the transaction which are not payable by the veteran or not disclosed in the loan package; and,

(d) Egregiously poor underwriting; e.g., approval of a loan without resolving obvious discrepancies in the loan package or despite the veteran's clear failure to meet VA's regulatory credit standards.

(2) Denial of liability for fraud or willful misrepresentation applies only to the original lender, and not to a "holder in due course." A holder in due course is one who acquired

the loan for value and did not participate in or have notice of the fraud or misrepresentation. A holder that acquired a loan from the original lender in a delinquent status is not considered a holder in due course by VA.

c. **Non-Willful Misrepresentation.** There is no basis for denial of liability by VA when apparent misrepresentation occurs without the willful complicity of the lender, or when the loan was acquired by a holder in due course. These include cases of relatively minor errors in judgment in processing the loan application resulting from misunderstandings of the lender, and cases in which the veteran or some other party intentionally misinforms the lender as to facts used in underwriting the loan and in which prudent underwriters would not find a basis for questioning the information. If the misrepresentation or error is material to approval of the loan and it is determined that knowledge of it was available to the lender prior to closing, VA may reduce its claim liability to the extent that it can be shown to have been increased by the misrepresentation or error.

d. **Violation of VA Requirements**

(1) To the extent that a holder fails to comply with VA servicing requirements, regulations and/or laws applicable to the servicing and origination of GI loans, a claim under Loan Guaranty is subject to adjustment by VA. VA' s general policy in determining the amount of the adjustment is to estimate the dollar amount by which the holder's failure to comply increased the claim payable on the loan. The claim is then adjusted by a corresponding amount. For example: if a holder inadvertently released an obligor from liability, and the obligor willfully defaulted as a result or VA lost a right to pursue collection against the obligor after loan termination, VA would adjust the claim payable to zero (38 CFR 36.4324(f) and 36.4325(b)(1)). Another example: If the holder's failure to obtain a valid lien at loan origination delayed foreclosure of the loan by 10 months, the holder's claim would be reduced by accrued interest and incurred advances and expenses during the 10 month period.

(2) The most common claim adjustments are for failure to report loan defaults timely (38 CFR 36.4315(a)) and failure to begin and prosecute liquidation (38 CFR 36.4319(f)) timely. Adjustments for failure to obtain adequate insurance settlements of hazard losses and to ensure that the settlements are applied to the loan balance or to restoration of the security are not unusual. Most claim adjustments are completely avoidable if holders are familiar with VA's requirements for servicing and liquidating VA-guaranteed loans and maintain internal control systems that monitor compliance. These standards are not significantly different than those expected by FNMA (Federal National Mortgage Association), FHLMC (Federal Home Loan Mortgage Corporation), GNMA (Government National Mortgage Association) and private mortgage insurors. Holders that make an effort to achieve familiarity with VA's requirements and maintain high standards of compliance will benefit, as will veterans and VA.

e. **Debarment**

(1) VA is authorized under section 3704(d) of title 38, United States Code, to debar a holder when a determination has been made that the holder has failed to:

(a) Maintain adequate loan accounting records; or,

(b) Demonstrate proper ability to service loans adequately.

(2) Under 38 CFR part 44, these debarments can be made effective Government-wide. Under 38 CFR 44.305, debarment may also be imposed based on conviction or civil judgment for fraud or criminal offenses, and for willful violation of a statutory or regulatory provision. This includes a willful failure to comply with VA's servicing procedures (38 CFR 36.4346).

(3) Any debarment action will be preceded by a written notice of intention to debar which will detail the servicing deficiencies or other misconduct found by VA. The holder will be given the opportunity to respond in writing and at a personal hearing before action is taken.

6.07 Payment and Final Accounting

a. **Advice to Holder.** When the claim is vouchered for payment, a notice will be sent to the holder/servicing agent together with a copy of VA's Analysis of Account and Claim (figs. 6-2 and
6-3).

b. **Return of Evidence of Guaranty.** Immediately following the receipt of a claim payment, the Loan Guaranty Certificate must be returned to VA marked "Canceled" over an official signature of the holder.

c. **Record Retention.** VA regulations do not require holders to retain records for any fixed period of time after a claim is paid. It is recommended that they be retained for 3 years.

6.08 Supplemental Claim

A supplemental claim may be filed for any items omitted from the original claim or paid for after it was submitted, or to contest a disallowance on the original claim. It is not necessary to use VA Form 26-1874, but a supplemental claim must be supported by the same documents required for the initial claim, such as receipts. A supplemental claim will be processed in the same manner as an initial claim.

CONTENTS

APPENDIXES

LOAN GUARANTY SERVICE
REGIONAL OFFICE ADDRESS LIST

State	Address/Phone Number
Alabama	VA Regional Office 474 South Court St. Montgomery, AL 36104 (205)223-7187
Alaska	VAOC/Regional Office 2925 Debarr Road Anchorage, AK 99508 (907)257-4736
Arizona	VA Regional Office 3225 North Central Ave. Phoenix, AZ 85012 (602)640-2745
Arkansas Regional	VA Regional Office P. O. Box 1280 Building 65, Fort Roots North Little Rock, AR 72115 (501)370-3760
California	VA Regional Office Federal Building 11000 Wilshire Blvd. Los Angeles, CA 90024 (310)575-7192 VA Regional Office Oakland Federal Building 1301 Clay Street Oakland, CA 94612-5209 (510)637-1126
Colorado	VA Regional Office Box 25126 44 Union Boulevard Denver, CO 80225
Connecticut	Loan Guaranty consolidated with Manchester, NH
Delaware	Loan Guaranty consolidated with Philadelphia, PA
Washington, D.C.	VA Regional Office 941 North Capitol St., N.E. Washington, D.C. 20421 (202)208-1318
Florida	VA Regional Office P.O. Box 1437 St. Petersburg, FL 33731 (813)893-3812
Georgia	VA Regional Office 730 Peachtree St., N.E. Atlanta, GA 30365 (404)347-3488
Hawaii	VA Medical and Office Center P.O. Box 50188 Honolulu, HI 96850 (808)541-1480
Idaho	VA Regional Office 805 Franklin Street Boise, ID 83702-5560
Illinois	VA Regional Office 536 South Clark Street P.O. Box 8136 Chicago, IL 60680 (312)353-4056
Indiana	VA Regional Office 575 N. Pennsylvania Street Indianapolis, IN 46204 (317)226-6681
Iowa	VA Regional Office 210 Walnut Street Des Moines, IA 50309 (515)284-4657

State	Address/Phone Number
Kansas	VA Medical and Regional Office Center 5500 E. Kellogg Wichita, KS 67218 (316)688-6720
Kentucky	VA Regional Office 545 South 3rd Street Louisville, KY 40202 (502)582-6025
Louisiana	VA Regional Office 701 Loyola Avenue New Orleans, LA 70113 (504)589-6412
Maine	Loan Guaranty consolidated with Manchester, NH
Maryland	VA Regional Office Federal Building 31 Hopkins Plaza Baltimore, MD 21201 (410)962-4250
Massachusetts	Loan Guaranty consolidated with Manchester, NH
Michigan	VA Regional Office 477 Michigan Ave. Detroit, MI 48226 (313)226-4224
Minnesota	VA Regional Office and Insurance Center One Federal Drive Fort Snelling, MN 55111 (612)725-3064
Mississippi	VA Regional Office 100 West Capitol Street Jackson, MS 39269 (601) 965-4825
Missouri	VA Regional Office 1520 Market Street St. Louis, MO 63103 (314) 539-3147
Montana	VA Medical and Regional Office Center Fort Harrison, MT 59636

State	Address/Phone Number
Nebraska	VA Regional Office 5631 S. 48th Street Lincoln, NE 68516 (402)437-5032
Nevada	Loan Guaranty consolidated with Oakland, CA
New Hampshire	VA Regional Office 275 Chestnut Street Manchester, NH 03101 (603)666-7527
New Jersey	VA Regional Office 20 Washington Place Newark, NJ 07102 (201)645-3470
New Mexico	VA Regional Office 500 Gold Avenue, S.W. Albuquerque, NM 87102 (505)766-2209
New York	VA Regional Office Federal Building 111 West Huron Street Buffalo, NY 14202 (716)846-5291 VA Regional Office 252 Seventh Avenue at 24th Street New York, NY 10001 (212)620-6421
North Carolina	VA Regional Office 251 North Main Street Winston-Salem, NC 27155 (919)631-5447
North Dakota	Loan Guaranty consolidated with Fort Snelling, MN
Ohio	VA Regional Office 1240 East 9th Street Cleveland, OH 44199 (216)522-3614
Oklahoma	VA Regional Office 125 S. Main Street Muskogee, OK 74401 (918)687-2158

(406) 447-7901

State	Address/Phone Number
Oregon consolidated	VA Regional Office Federal Building 1220 S.W. Third Avenue Portland, OR 97204 (503)326-2475
Pennsylvania	VA Regional Office and Insurance Center 5000 Wissahickon Avenue P.O. Box 8079 Philadelphia, PA 19101 (215)951-7847 VA Regional Office 1000 Liberty Avenue Pittsburgh, PA 15222 (412)644-6660
Puerto Rico	VA Regional Office GPO Box 4867 San Juan, PR 00936 (809)766-5120
Rhode Island	Loan Guaranty consolidated with Manchester, NH
South Carolina	VA Regional Office 1801 Assembly Street Columbia, SC 29201 (803)765-5616
South Dakota	Loan Guaranty consolidated with Fort Snelling, MN
Tennessee	VA Regional Office 110 9th Avenue, S. Nashville, TN 37203 (615)736-5243
Texas	VA Regional Office 8900 Lakes at 610 Drive Houston, TX 77054 (713)660-4134 VA Regional Office 1400 N. Valley Mills Drive Waco, TX 76799 (817)757-6822
Utah	VA Regional Office P.O. Box 11500 Salt Lake City, UT 84147 (801)524-5983
Vermont	Loan Guaranty with Manchester, NH
Virginia	VA Regional Office 210 Franklin Road, S.W. Roanoke, VA 24011 (703)982-4736
Washington	VA Regional Office Federal Building 915 Second Avenue Seattle, WA 98147 (206)220-6126
West Virginia	VA Regional Office 640 4th Avenue Huntington, WV 25701 (304)529-5414
Wisconsin	VA Regional Office Building 6 5000 West National Avenue Milwaukee, WI 53295 (414)382-5050
Wyoming	Loan Guaranty consolidated with Denver, CO

**(EXTRACT OF CIRCULAR 26-93-14,
DATED JULY 7, 1993)**

VA LOAN IDENTIFICATION NUMBERS

1. **GENERAL**. As part of the Veterans Benefits Administration ADP (Automatic Data Processing) modernization effort, Loan Guaranty Service is updating its information and production systems. This effort includes, but is not limited to, the recently installed LP (Loan Processing) system, the LFF (Lockbox and Funding Fee) reporting system and the LCS (Liquidation and Claims System). One functional requirement of the Loan Guaranty modernization project is to integrate all automated systems so that data can be shared across applications and support EDI (Electronic Reporting and Electronic Data Interchange.)

2. **VA LOAN IDENTIFICATION NUMBER**

a. Electronic reporting of GI loan default, liquidation, claim and other information will be of great benefit to both VA and the loan servicing community. VA is actively supporting development of EDI standards for the mortgage industry. However, a method of accurately identifying the loan in VA's and the servicer's systems of records must be implemented before electronic reporting will be practical. Since the servicer's loan number may change each time the loan is sold on the secondary mortgage market and VA's internal loan identification number does not change, the logical choice as a common identifier is VA's loan identification number.

b. Under the Loan Guaranty Program a VA loan number has been entered and displayed in a number of different configurations. These differences have even extended to the various Loan Guaranty automated systems. This has caused problems in a number of areas including the reporting of default information by servicers and holders. To correct these problems VA has developed a 12 position numeric VA LIN (Loan Identification Number) that allows VA to accurately track a loan record across its systems. (At some future date VA LIN may be extended to l3-digits to accommodate a check digit.)

3. **DEFINITIONS**. The VA loan identification number consists of the following four subfields:

a. **OJ (Office of Jurisdiction)**. A two-position numeric field which identifies the regional office that currently has responsibility for the loan. OJ may change over the life of the loan due to changes in the areas of responsibility assigned to a specific regional office.

b. **OO (Office of Origin)**. A two-position numeric field which identifies the regional office which had jurisdiction for the area within which the property securing the loan was located at the time the loan closed. The OO assigned to a given loan does not change regardless of shifts in areas of responsibilities or office consolidations.

c. **LT (Loan Type)**. This is a one-position field identifying the Federal legislation which authorized VA to guarantee the loan and the fund backing the loan. This value is used for VA's internal accounting and ensures the uniqueness of the identifier as loan number (defined below) may be duplicated within OO. With the exception of guaranteed loans which are being refunded (purchased) by VA, loan type does not change.

d. **Loan Number**. A seven-position serial number assigned to the loan by the OO. Since each regional office traditionally assigned direct, GI and vendee loan numbers from separate but overlapping registers, loan numbers may be duplicated within OO, but are unique to the OJ-OO-loan type combination. In this case the loan number does not change.

4. **DETERMINING THE CORRECT VA LOAN IDENTIFICATION NUMBER**. The 12 position VA loan identification number is currently provided to lenders via the LP system which prints the full VA loan identification number on Loan Guaranty certificates and other correspondence. Also, areas served by the St. Petersburg, Waco, Cleveland and Washington D.C. Regional Offices receive certificates of reasonable value and other correspondence utilizing the 12 position loan number as generated by the automated Construction and Valuation systems installed at those offices. All other VA output is being reviewed and revised to include the 12 position VA loan identification number where appropriate. The following paragraphs describe how a VA loan identification number may be constructed in those instances where it has not been provided to program participants.

5. **HOW TO DETERMINE THE CORRECT OJ**

a. Servicers can, using information available in their own system of records, develop an accurate 12 position VA loan identification number for most GI loans in their inventory. This process begins with the determination of the correct VA office of jurisdiction for the guaranteed loan.

b. Servicers may use the geographic location of the property securing the loan to determine the current OJ. Each OJ is assigned to a specific geographic area. Most OJs are responsible for the area in a single State. A list of all current OJs and their areas of responsibility is found in exhibit A. This list is arranged alphabetically by State and references the current office of jurisdiction for subdivisions of the State when the entire State is not under the jurisdiction of a single regional office.

c. To determine the office of jurisdiction for a particular loan, first ascertain the location of the property securing the loan; then check that location against exhibit A. For example, a
property securing a loan is located in South Dakota. Regional office number 35, St. Paul, MN, is the current OJ for South Dakota; so OJ equals 35.

6. **HOW TO DETERMINE THE CORRECT OO**

a. Office consolidations and territory changes have resulted in some OJs which administer loans with different OOs. Since most consolidations occurred more than 30 years ago, this is not a major problem. However, to determine the correct OO for the situations where the consolidations occurred in the past 30 years, the following rules apply:

(1) If the OJ for a loan is one of the following, the OO is the same as the OJ:

06	09	10	11	13	14	15	16	17	18	19	20	21	22
23	25	26	27	28	29	30	31	34	36	39	40	41	43
44	45	46	47	48	49	50	51	52	55	59	62	63	72

(2) If the OJ is one of the these three stations, the following rules apply:

07 Buffalo	If the loan is secured by a property in Wayne County, New York, and the date of the loan is prior to January 1, 1983, the OO is 06. Otherwise the OO is 07.
35 St. Paul	If the loan is secured by a property in South Dakota and the date of the loan is prior to May 1, 1962, the OO is 38. Otherwise the OO is 35.
73 Manchester	If the loan is secured by a property in Massachusetts or Rhode Island and the date of the loan is prior to June 1, 1990, the OO is 01. If the loan is secured by a property in Maine and the date of the loan is prior to December 7, 1990, the OO is 02. If the loan is secured by a property in Vermont and the date of the loan is prior to October 1, 1984, the OO is 05. If the loan is secured by a property in Connecticut and the date of the loan is prior to June 1, 1990, the OO is 05. Otherwise the OO is 73.

b. Occasionally, lenders, servicers or holders need to determine the correct OO for a loan which was closed prior to 1962. Regional office personnel may assist in making this determination by reviewing the appropriate loan record in the LGY INDEX. Exhibit B is a listing by OJ which shows the allowable OOs for a given OJ. This exhibit contains all valid combinations taking into consideration territorial changes and office combinations since the beginning of the program.

7. HOW TO DETERMINE THE CORRECT LT

a. Lenders, servicers and holders generally only originate, service and hold VA guaranteed loans. A few servicers and holders are involved with VA vendee loans which have been sold to private sector investors. Thus, while most servicers and holders have only the two loan types designating guaranteed loans in their portfolios, some may have portfolios containing several VA loan types. Exhibit C defines all VA loan types.

(l) If the loan is a VA guaranteed loan the following rules are used to determine the correct loan type:

Loan Type 2	If the security for the loan is a manufactured home and the loan was processed under the provisions of Title 38, U. S. Code, section 37l2, the loan type is always 2. If the security for the loan is not a manufactured home and the loan closed prior to January 1, 1990, the loan type is 2.
Loan Type 6	If the security for the loan is not a manufactured home and the loan closed on or after January 1, 1990, the loan type is 6.

(2) In addition to guaranteed loans, servicers and holders may have VA vendee loans which VA has sold in the past. Presently these loans are designated by two loan types. Vendee loans where the antecedent loan was a VA direct loan are loan type 3. Vendee

loans where the antecedent loan was a VA guaranteed loan financed through LGRF (Loan Guaranty Revolving Fund) are loan type 4. Vendee loans where the antecedent loan was a VA guaranteed loan financed through GIF (Guaranty Indemnity Fund) have not been sold by VA through 1992 but may be sold in the future. The loan type for these loans is 7. Also, a few loans made under the provisions of VA Direct Loan Program were sold with repurchase agreements rather than being converted to guaranteed loans. The loan type for these loans is l. The documentation which accompanied loans sold by VA identifies the loan type.

(3) In addition to the loan types associated with loans which may be held in the private sector, VA continues to hold in its portfolio direct loans (loan type 1) it has made in the past, and acquired loans (loan type 5 (LGRF) and loan type 8 (GIF)) it has refunded in the past.

8. HOW TO DETERMINE THE CORRECT LOAN NUMBER

a. There were 13 million GI loans guaranteed prior to deployment of LP. For each of these cases, the loan number is printed on the Loan Guaranty certificate issued by VA. That document should be used to determine the correct loan number segment of a VA loan identification number.

b. Traditionally, the loan number for VA guaranteed loans has been referred to as the "LH number" since the letters "LH" or some variation such as "LHM" (manufactured home) or "LHR" (refinancing loan) have been used as a prefix to the actual number itself. In addition to those prefixes, suffixes have often been appended to the loan number. Neither prefixes or suffixes to the loan number should be used in constructing a VA loan identification number.

c. Since the loan number portion of a VA loan identification number is a seven-position numeric value, loan numbers found on Loan Guaranty certificates and other documents should be expanded to seven positions in the event they are less than seven positions. This is accomplished by appending leading zeros to the existing loan number.

9. STORAGE AND DISPLAY OF THE VA LOAN IDENTIFICATION NUMBER

To construct a VA LIN, the four subfields are combined in OJ-OO-LT-loan number order. The full l2 position number forms a unique identifier within VA's system of records. It may be displayed as 12 contiguous positions or with the components separated by either dashes or spaces. It is always stored in VA ADP systems as l2 contiguous positions.

LOAN GUARANTY REGIONAL OFFICE JURISDICTIONS
GEOGRAPHIC JURISDICTIONS

State or Political Subdivision	Regional Office
AL Entire State	22 Montgomery, AL
AK Entire State	63 Anchorage, AK
AR Entire State	50 Little Rock, AR
AZ Entire State	45 Phoenix, AZ
CA 11 counties: Imperial, Inyo, Kern, Los Angeles, Orange, Riverside, San Bernadino, San Diego, San Luis Obispo, Santa Barbara, Ventura	44 Los Angeles, CA
CA All counties except those under Los Angeles	43 San Francisco, CA
CO Entire State.	39 Denver, CO
CT Entire State.	73 Manchester, NH
DE Entire State.	10 Philadelphia, PA
DC Entire district.	72 Washington, DC
FL Entire State.	17 St. Petersburg, FL
GA Entire State.	16 Atlanta, GA
HI Entire State.	59 Honolulu, HI
ID Entire State.	47 Boise, ID
IL Entire State.	28 Chicago, IL
IN Entire State.	26 Indianapolis, IN
IA Entire State.	33 Des Moines, IA
KS Entire State.	52 Wichita, KS
KY Entire State.	27 Louisville, KY
LA Entire State.	21 New Orleans, LA
ME Entire State.	73 Manchester, NH

LOAN GUARANTY REGIONAL OFFICE JURISDICTIONS
GEOGRAPHIC JURISDICTIONS

State or Political Subdivision	Regional Office
MD All counties except those under Washington, DC.	13 Baltimore, MD
MD 2 counties: Montgomery, Prince Georges.	72 Washington, DC
MA Entire State.	73 Manchester, NH
MI Entire State.	29 Detroit, MI
MN Entire State.	35 St. Paul, MN
MS Entire State.	23 Jackson, MS
MO Entire State.	31 St. Louis, MO
MT Entire State.	36 Ft. Harrison, MT
NE Entire State.	34 Lincoln, NE
NV 2 counties: Clark, Lincoln.	44 Los Angeles, CA
NV All counties except those under Los Angeles.	43 San Francisco, CA
NH Entire State.	73 Manchester, NH
NJ Entire State.	09 Newark, NJ
NM Entire State.	40 Albuquerque, NM
NY 14 counties: Allegany, Cattaraugus, Chautauqua, Erie, Genesee, Livingston, Monroe, Niagara, Ontario, Orleans, Steuben, Wayne, Wyoming, Yates.	07 Buffalo, NY
NY All counties not assigned to Buffalo.	06 New York, NY
NC Entire State.	18 Winston-Salem, NC
ND Entire State.	35 St. Paul, MN
OH Entire State.	25 Cleveland, OH
OK Entire State.	51 Muskogee, OK
OR Entire State.	48 Portland, OR

LOAN GUARANTY REGIONAL OFFICE JURISDICTIONS
GEOGRAPHIC JURISDICTIONS

State or Political Subdivision	Regional Office
PA 40 counties: Adams, Berks, Bradford, Bucks, Cameron, Carbon, Centre, Chester, Clinton, Columbia, Cumberland, Dauphin, Delaware, Franklin, Juniata, Lackawanna, Lancaster, Lebanon, Lehigh, Luzerne, Lycoming, Mifflin, Monroe, Montgomery, Montour, Northampton, Northumberland, Perry, Philadelphia, Pike, Potter, Schuylkill, Snyder, Sullivan, Wayne, Wyoming, York.	10 Philadelphia, PA
PA 27 counties not assigned to Philadelphia.	11 Pittsburgh, PA
PR Entire Commonwealth.	55 San Juan, PR
RI Entire State.	73 Manchester, NH
SC Entire State.	19 Columbia, SC
SD Entire State.	35 St. Paul, MN
TN Entire State.	20 Nashville, TN
TX 90 counties: Angelina, Aransas, Atascosa, Austin, Bandera, Bee, Bexar, Blanco, Brazoria, Brewster, Brooks, Caldwell, Calhoun, Cameron, Chambers, Colorado, Comal, Crockett, DeWitt, Dimmit, Duval, Edwards, Fort Bend, Frio, Galveston, Gillespie, Goliad, Gonzales, Grimes, Guadalupe, Hardin, Harris, Hays, Hidalgo, Houston, Jackson, Jasper, Jefferson, Jim Hogg, Jim Wells, Karnes, Kendall, Kenedy, Kerr, Kimble, Kinney, Kleberg, LaSalle, Lavaca, Liberty, Live Oak, McCulloch, McMullen, Mason, Montgomery, Nacogdoches, Newton, Nueces, Orange, Pecos, Polk, Real, Refugio, Sabine, San Augustine, San Jacinto, San Patricio, Schleicher, Shelby, Starr, Sutton, Terrell, Trinity, Tyler, Uvalde, Val Verde, Victoria, Walker, Waller, Washington, Webb, Wharton, Willacy, Wilson, Zapata, Zavala.	62 Houston, TX

LOAN GUARANTY REGIONAL OFFICE JURISDICTIONS
GEOGRAPHIC JURISDICTIONS

State or Political Subdivision	Regional Office
TX City of Texarkana.	50 Little Rock, AR
TX All counties except those assigned to Houston, TX, and the city of Texarkana, TX, assigned to Little Rock, AR.	49 Waco, TX
UT Entire State.	41 Salt Lake City, UT
VT Entire State.	73 Manchester, NH
VA 6 counties: Arlington, Fairfax, Loudoun, Prince William, Stafford, Spotsylvania, and 4 independent VA cities: Alexandria, Fairfax, Falls Church, Fredericksburg.	72 Washington, DC
VA Entire state except the 6 counties and 4 independent cities assigned to Washington, DC.	14 Roanoke, VA
VI All US Virgin Islands.	55 San Juan, PR
WA 3 counties: Clark, Klickitat, Skamania.	48 Portland, OR
WA Entire State except 3 counties assigned to Portland, OR.	46 Seattle, WA
WV 4 counties: Brooke, Hancock, Marshall, Ohio.	11 Pittsburgh, PA
WV Entire State except 4 counties assigned to Pittsburgh, PA.	15 Huntington, WV
WI Entire State.	30 Milwaukee, WI
WY Entire State.	39 Denver, CO
Pacific Islands of: American Samoa, Guam, Wake, Midway, Commonwealth of Northern Mariana Islands.	59 Honolulu, HI

HISTORICAL LISTING OF VALID OFFICE OF JURISDICTION OFFICE OF ORIGIN COMBINATIONS SINCE THE BEGINNING OF THE PROGRAM

OJ	OO	STATION NAME
06	06	New York, NY
	57	Albany, NY
	70	Brooklyn, NY
	71	Syracuse, NY
07	07	Buffalo, NY
	06	New York, NY
09	09	Newark, NJ
10	10	Philadelphia, PA
	13	Baltimore, MD
	56	Wilkes-Barre, PA
	60	Wilmington, DE
11	11	Pittsburgh, PA
13	13	Baltimore, MD
	60	Wilmington, DE
14	14	Roanoke, VA
15	15	Huntington, WV
16	16	Atlanta, GA
17	17	St. Petersburg, FL
	69	Miami, FL
18	18	Winston-Salem, NC
19	19	Columbia, SC
20	20	Nashville, TN
21	21	New Orleans, LA
	66	Shreveport, LA
22	22	Montgomery, AL
23	23	Jackson, MS
25	25	Cleveland, OH
	24	Cincinnati, OH
26	26	Indianapolis, IN
27	27	Louisville, KY
28	28	Chicago, IL
	90	Springfield, IL
29	29	Detroit, MI
30	30	Milwaukee, WI
31	31	St. Louis, MO
	32	Kansas City, MO
33	33	Des Moines, IA
34	34	Lincoln, NE
35	35	St. Paul, MN
	37	Fargo, ND
	38	Sioux Falls, SD
36	36	Ft. Harrison, MT
39	39	Denver, CO
	42	Cheyenne, WY
40	40	Albuquerque, NM
41	41	Salt Lake City, UT
43	43	San Francisco, CA
	54	Reno, NV
44	44	Los Angeles, CA
	64	San Diego, CA
45	45	Phoenix, AZ
46	46	Seattle, WA
47	47	Boise, ID
48	48	Portland, OR
	46	Seattle, WA
49	49	Waco, TX
	61	Dallas, TX
	65	Lubbock, TX

HISTORICAL LISTING OF VALID OFFICE OF JURISDICTION OFFICE OF ORIGIN COMBINATIONS SINCE THE BEGINNING OF THE PROGRAM

OJ	OO	Station Name
50	50	Little Rock, AR
51	51	Muskogee, OK
	67	Oklahoma City, OK
52	52	Wichita, KS
	32	Kansas City, KS
55	55	San Juan, PR
59	59	Honolulu, HI
	59	Guam, GU
62	62	Houston, TX
	53	San Antonio, TX
63	63	Anchorage, AK
72	72	Washington, DC
73	73	Manchester, NH
	01	Boston, MA
	02	Togus, ME
	05	White River, VT
	08	Hartford, CT

LOAN TYPE DEFINITIONS

Type	Definition
0	Withdrawn or rejected direct loan application dated 1950 through 1955.
1	Direct loan. Underwritten and made by VA. Associated with either the DLRF (Direct Loan Revolving Fund) or the NALF (Native American Loan Fund).
2	GI loan associated with the LGRF.
3	Vendee loan associated with the DLRF (e.g. foreclosed DL).
4	Vendee loan associated with the LGRF (type 2 GI).
5	Acquired loan associated with the LGRF (refunded type 2 GI) or the DLRF (repurchased previously sold type 1 direct loan).
6	Guaranteed loan associated with GIF.
7	Vendee loan associated with the GIF (type 6 GI).
8	Acquired loan associated with GIF (refunded type 6 loan).

NOTE: Loan types 5 and 8 are used only within VA. Servicers should not have any of these loans in their portfolio.

a. Loan types 1, 3 and 4 were sold in the past, other types may be sold in the future.

b. When VA refunds a GI loan from the LGRF Fund or a previously sold direct loan, the loan type is changed to 5 and the remainder of the loan identification number is kept constant. This change is internal to VA.

c. When VA refunds a GI loan from the GIF, the loan type is changed to 8, and the remainder of the loan identification number is kept constant. This change is internal to VA.

(EXTRACT OF CIRCULAR 26-90-11 DATED MARCH 6, 1990)

LOAN FILE SETUP

Lenders are expected to process and close loans in accordance with VA regulations, directives and policies. Increasingly, lenders originating VA guaranteed loans operate in more than one geographic area but underwrite from a central or regional location. It is important that our instructions to lenders be consistent. Because of the numerous different local releases to lenders from field stations concerning loan file setup, standardized submissions for prior approval loan applications, prior approval loan closings and automatic loans, have been developed. These standardized loan file setups will be for nationwide usage.

LOAN DOCKET SETUP FOR PRIOR APPROVAL LOAN APPLICATIONS

1. Lender's cover letter (if used).

2. VA Form 26-8320, Certificate of Eligibility

3. VA Forms 26-1802a, VA Application for Home Loan Guaranty

4. VA Form 26-8923, Interest Rate Reduction Refinancing Loan Worksheet (if applicable)

5. VA Form 26-8937, Verification of VA Benefit-Related Indebtedness

6. VA Form 26-0503, Federal Collection Policy Notice (at application or closing)

7. VA Form 26-6393, Loan Analysis (if used)

8. Original credit report and any related documents; e.g., proof of debt payment, explanations, etc.

9. VA Form 26-8497a, Request for Verification of Deposit and other related documents

10. VA Form 26-8497, Request for Verification of Employment; verification(s) of other income (e.g., pay stubs, tax returns, profit and loss statement and balance sheet)

11. Purchase/Earnest money contract

12. Copy of VA Form 26-1843a, Master Certificate of Reasonable Value (if applicable)

13. Remaining documents - no particular order

LOAN DOCKET SETUP FOR PRIOR APPROVAL LOAN CLOSINGS

1. Lender's cover letter or transmittal letter (if used)

2. VA Forms 26-1820, Report and Certification of Loan Disbursement

3. VA Form 26-8923, Interest Rate Reduction Refinancing Loan Worksheet (if applicable)

4. VA Form 26-8998, Acknowledgment of Receipt of Funding Fee from Mortgagee; and when applicable, VA Form 26-0500, Notification to Mortgagee of Funding Fee Shortage, and VA Form 26-8999, Acknowledgment of Receipt of Funding Fee Shortage to Mortgagee

5. VA Form 26-0551, Debt Questionnaire (not applicable if VA Form 26-1802a, VA Application for Home Loan Guaranty, is used)

6. VA Form 26-0503, Federal Collection Policy Notice (at application or closing)

7. HUD-1 Settlement Statement

8. CRV requirements; e.g., warranty, final inspection, termite certification, etc.

9. VA Form 26-1859, Warranty of Completion of Construction in Substantial Conformity with Approved Plans and Specifications (new construction only)

LOAN DOCKET SETUP FOR AUTOMATIC LOANS

1. Lender's cover letter or transmittal letter (if used)

2. VA Form 26-8320, Certificate of Eligibility

3. VA Form 26-1820, Report and Certification of Loan Disbursement

4. VA Form 26-8923, Interest Rate Reduction Refinancing Loan Worksheet (if applicable)

5. VA Form 26-8998, Acknowledgment of Receipt of Funding Fee for Mortgagee; and when applicable, VA Form 26-0500, Notification to Mortgagee of Funding Fee Shortage and VA Form 26-8999, Acknowledgment of Receipt of Funding Fee Shortage to Mortgagee

6. VA Form 26-8937, Verification of VA Benefit-Related Indebtedness

7. VA Form 26-0551, Debt Questionnaire (not applicable if VA Form 2601802a, VA Application for Home Loan Guaranty, is used)

8. VA Form 26-0503, Federal Collection Policy Notice.

9. HUD-1 Settlement Statement

10. CRV requirements; e.g., final compliance inspection report, termite certification, private road requirements, evidence of enrollment in 10 year insurance-backed protection plan

11. VA Form 26-1859, Warranty of Completion of Construction in Substantial Conformity with Approved Plans and Specifications (new construction only)

12. Veteran's loan application to lender or VA Form 26-1802a, VA Application for Home Loan Guaranty (if used)

13. VA Form 26-6393, Loan Analysis (if used)

14. Original credit report and any related documents; e.g., proof of debt payment, explanation, etc.

15. VA Form 26-8497a, Request for Verification of Deposit, and other related documents

16. VA Form 26-8497, Request for Verification of Employment; verification(s) of other income (e.g., pay stubs, tax returns, profit and loss statement and balance sheet)

17. The veteran's written application for an interest rate reduction refinancing loan (if applicable)

18. Purchase/earnest money contract

19. Copy of VA Form 26-1843a, Master Certificate of Reasonable Value (if applicable)

20. Remaining documents - no particular order

(EXTRACT OF CIRCULAR 26-90-32, DATED AUGUST 23, 1992)

FORBEARANCE ON VA HOME LOANS DURING SPECIAL MILITARY ACTIONS AND SOLDIERS' AND SAILORS' CIVIL RELIEF ACT OF 1940, AS AMENDED

1. When members of the United States Armed Forces are required to make immediate departures for distant lands in order to protect our nation's interests, many military members are routinely prepared for family separations and related financial rearrangements. However, some orders may come with such limited advance warning that difficulties may arise for spouses who must remain and manage households.

2. It has been the longstanding policy of the Department of Veterans Affairs to encourage loan holders to extend all reasonable forbearance in the event a borrower becomes unable to meet the terms of a VA loan. This policy is especially appropriate when delinquencies may be the direct result of family disruptions due to special military actions.

3. Financial difficulties may be even more severe in such situations for members of the Reserves or National Guard who may be unforseeably called to active duty for extended periods of time. If it appears that more than simple forbearance is warranted, VA regulations allow holders considerable latitude in modifying the terms of a loan to prevent foreclosure and help the borrower to retain and pay for his or her home. Such modifications may include loan extension, reamortization and interest rate reduction refinancing to prevent and/or cure a default.

4. Members of the Reserves or National Guard who have home loans and are called to active military service are also entitled to protection under the provisions of the Soldiers' and Sailors' Civil Relief Act of 1940, as amended (50 U.S.C. App. sections 501-590). While the Act does not generally apply to obligations incurred during a current period of active military service, provisions may cover veteran-borrowers on active duty with respect to obligations they have incurred prior to their current period of service. In order for a veteran to qualify for the protections available under the Act, his or her obligation has to have originated prior to the current period of active military service (i.e., during a period of break in service between active duty tours or during a periods of active military service which was followed by a break in service) and, in the case of a secured loan obligation, the property must still be owned by him or her during the current period of active service. Benefits under the Act may also extend to co-obligors on a loan.

5. The purpose of the Act is to promote and strengthen the national defense by suspending enforcement of certain civil liabilities of certain persons serving in the armed forces. Therefore, when a veteran-borrower's ability to meet his or her obligations has been impaired due to military service, certain relief is afforded against the penalties that would otherwise be imposed for nonpayment of such obligations. In addition, the relief

provisions include the right, in some cases, to make reduced payments on obligations and protections through the courts against foreclosure.

6. VA is not charged with enforcement of the Act, but will perform its mission of serving veterans by making every effort to ensure that they receive the protections to which they are entitled. Moreover, it is not VA's responsibility to provide legal advice to veterans or loan holders with respect to requirements of the Act. We do, however, consider certain provisions of the Act to be important to program participants and the following, while not intended to be substituted for the advice of counsel, is designed to inform program participants in a general way about provisions of the law.

a. **Six Percent Interest Rate Limitation**. When the Act applies (as described in paragraph 4), any obligation or liability, such as a home loan, bearing interest at a rate in excess of 6 percent per annum is, during the veteran's period of active duty, reduced to a rate of no more than 6 percent (50 U.S.C. App. 526). The rate cap of 6 percent is calculated to include any fees or other charges otherwise payable on the loan (e.g., late charges).

(1) The Act is silent as to any actions which the veteran must take to begin payments at the lower rate. Absent a specific requirement, veterans (or their spouses, other co-obligors or legal representatives) should, however, be encouraged to notify their loan holder before beginning payments at the reduced rate. Veterans should also be encourage to cooperate with their loan holders by providing information which will help demonstrate their eligibility for benefits available under the Act. Loan holders are cautioned to review their payment processing procedures in order to ensure that payments in the amount allowable under the Act are not inappropriately returned to borrowers as insufficient, even though no prior notice may have been received. Loan holders should also be prepared to respond to inquiries from veterans as to the amount of the monthly installment payment which would be required at a 6 percent interest rate and to provide revised payment cards or coupon books when appropriate.

(2) In order to restore application of the original interest rate on the note during an obligor's period of military service, the holder must apply to a court and show that the veteran's ability to repay the obligation has not been materially affected by military service. The court "may take such order as in its opinion may be just" with respect to the rate of interest due and payable.

(3) At the time the Act became law, an interest rate of 4 percent or less was typical for home loans. The fact that interest rates are currently substantially higher does not, however, affect the applicability of the Act.

(4) The Office of the General Counsel has determined that, for purposes of accounting between VA and a loan holder when a claim is filed under Loan Guaranty, VA's liability will not exceed the liability of the veteran. Since the veteran is not obligated to pay interest at a rate in excess of 6 percent, VA as guarantor is not obligated to include interest on the obligation in excess of 6 percent for the period of time that the veteran was

eligible under the provisions of the Act. However, if the holder obtained permission from a court of competent jurisdiction to obligate the veteran under the terms of the original obligation or to modify those terms, VA would be bound to honor the court's decision.

b. **Stay in Enforcement**. In addition to an interest rate reduction, the Act provides for a separate form of forbearance which a veteran can obtain through order of a court if he or she applies for it during his or her period of military service or within 6 months after separation (50 U.S.C. App. 590). If the court finds that the ability of the veteran to maintain the obligation has been materially affected by entry into military service, it can issue a stay in the enforcement of the obligation. The maximum period of the complete stay on payments would coincide with the veteran's period of military service. The court could then require that the creditor accept repayment of the delinquent principal and interest (computed at the note rate) as of the date of separation or the date the veteran applied to the court, whichever is later, in equal installments over a period of time equal to the remaining term of the loan plus the period of military service. A lesser repayment period could also be established if the court were to find such terms to be just; similarly, the court is not obligated to order a complete suspension of payments during the period of military service and could require the veteran to make regular partial payments prior to separation.

(1) The Act does not specifically relate relief under this provision to the interest rate reduction to which the veteran may be entitled. It is therefore unclear whether these provisions are mutually exclusive or may be combined.

(2) In view of the broad powers granted to courts to provide payment relief to military personnel, loan holders are encouraged to negotiate reasonable partial payment and repayment schedules with borrowers in order to minimize the need for costly and time-consuming litigation.

c. **Foreclosure**. Court permission is necessary to foreclose a loan that falls under the provisions of the Soldiers' and Sailors' Civil Relief Act of 1940, as amended. Foreclosure sales (or manufactured housing repossessions) during the veteran's period of military service or within 3 months thereafter will be invalid unless they take place pursuant to a written agreement between the parties involved or they are initiated "upon an order previously granted [the holder] by the court and a return thereto [is] made and approved by the court"; i.e., approval before proceeding with a power of sale foreclosure and subsequent court confirmation of sale may be necessary (50 U.S.C. App. 532).

(1) Many foreclosure actions require affidavits concerning the active duty military status of the obligors, and the accuracy of such items is very important in order to avoid title defects and possible penalties of imprisonment and/or fines for violations of the provision of the Act, or for attempts to violate its provisions.

(2) Loan holders are encouraged to become familiar with the Act in order to avoid losses associated with foreclosures which might actually be prevented through the

exercise of forbearance, and to ensure compliance with any restrictions on foreclosures which may apply in their particular areas of operation.

d. **Additional Stays**. A veteran-borrower can petition a court of competent jurisdiction during the period of military service or within 60 days thereafter to request any action or proceeding be stayed (50 U.S.C. App. 521). Furthermore, the veteran-borrower can petition a court for a complete stay against enforcement of the loan obligation (50 U.S.C. App. 590). Court determinations for any of these actions will weigh heavily upon whether or not the veteran-borrower's ability to discharge the obligation is materially affected by reason of his or her military service. However, nothing in the Act prevents modification or termination of loan agreements pursuant to a written agreement between the parties involved executed during or after the period of military service of the person concerned (50 U.S.C. App. 517).

e. **Rights of Redemption**. The Act places a different restriction on redemption periods than on foreclosure sales; namely, any statutory redemption period stops running during the veteran's current tour of military service and resumes after separation (50 U.S.C. App. 525). This restriction applies with respect to any redemption period which would otherwise run as a result of a foreclosure action against a person in military service, regardless of whether or not the mortgage was executed prior to the current period of service. The extension of a redemption period will clearly affect VA's ability to market property acquired subject to redemption; it will not, however, be considered a title defect which would make a conveyance unacceptable.

7. In general, the Act provides broad potential relief from obligations to persons in military service. With respect to an obligor who has entered military service and is subject to the Act, creditors must obtain either written agreement from the obligor or approval from a court in order to enforce their rights under a loan agreement. (Any written agreement obtained prior to the obligor's entry into military service may not provide a legal basis for enforcement of the creditor's rights.) In reaching a decision, the court will primarily be guided by consideration as to whether military service has affected the obligor's ability to maintain the obligation or answer an legal proceeding, such as foreclosure, brought by the creditor.

8. VA's advice to veterans and their families will encourage them to seek cooperation from their loan holders and to discuss other possibilities with private counsel and military attorneys, as necessary. VA is not in a position to offer legal advice to veterans or loan holders concerning requirements of the Act or possible interpretations by local courts. One source of such advice for veterans is Department of the Army Pamphlet 27-166, Soldiers' and Sailors' Civil Relief Act (August, 1981).

9. Holders should obtain opinions from their own counsel to ensure compliance with all provisions of the Act, as well as other local statutes requiring the extension of forbearance, so as not to invalidate a foreclosure. In some States, specific statutes have been enacted which have provisions which may be similar or identical to those found in the Act and, in some states, local statutes may afford obligors greater rights and

protections than those provided by the Act. Differences in interpretation on individual cases should be brought to the attention of the Office of the District Counsel and every effort should be made to reconcile such differences fairly and without disruption in program operations.

VA Foreclosure Timeframes

This is the timeframe used by the VARO of jurisdiction in calculating initial cutoff dates under 38 CFR 36.4319(f). It provides a reasonable allowance for completion of legal action. The timeframe represents the interval from referral to counsel to begin foreclosure until the completion of the action, assuming an uncontested foreclosure which is not delayed by publication because not all parties can be personally served. It may be extended when warranted by circumstances. The timeframes in this table are subject to change by local offices upon the advice of their District Counsel; any questions concerning them should be addressed to the appropriate local office. The legal procedure given below for each State is generally the most common procedure used. Where more than one action is cited, consult the VARO of jurisdiction to determine the circumstances under which each is appropriate.

Jurisdiction	**Procedure**	**FinalEvent**	**Timeframe**
Alabama	Sale with publication	Sale	45 days
Alaska	Non-judicial	Trustee's Sale	100 days
Arizona	Non-judicial	Trustee's Sale	3 months plus 1 week
Arkansas	Judicial with personal service	Commisioner's Sale	120 days
	Non-judicial	Sheriff's Sale	90 days
California	Non-judicial	Trustee's Sale	130 days
Colorado	Non-judicial	Public Trustee's Sale	90 days
Connecticut	Judicial Order:		
	Strict Foreclosure	Judicial Order	6 months
	Foreclosure by Sale	Committee Deed	6 months
Delaware	Judicial	Sheriff's Sale	4 months
District of Columbia	Non-judicial	Sale	60 days
Florida	Judicial	Confirmation	8 months
Georgia	Non-judicial	Sale	60 days*
*(First Tuesday of the month which is more than 30 and less than 60 days after referral)			
Hawaii	Judicial	Confirmation	6 months
Idaho	Non-judicial	Sale	5 months
Illinois	Judicial	Sheriff's Sale	7 months
Indiana			
(For loans closed on or after July 1, 1975)			
	Judicial	Sheriff's Sale	6 months
(For loans closed before July 1, 1975)			
	Judicial	Sheriff's Sale	9 months
Iowa	Judicial	Sheriff's Sale	7 months
Kansas	Judicial	Sheriff's Sale	20 weeks
Kentucky	Judicial	Confirmation of Sale by the Account	5 months
Louisiana	Judicial by Executor Process	Sheriff's Sale	5 months
Maine	Judicial Order:		
	Strict Foreclosure	Judicial Order	20 months
	Foreclosure by Sale	Deed	8 months
Maryland	Judicial	Trustee's Sale	90 days
Massachusetts	Judicial Order	Sale and Deed	10 months
Michigan	Non-judicial	Sheriff's Sale	75 days

Minnesota	Non-judicial	Sheriff's Sale	12 weeks
Mississippi	Non-judicial	Trustee's Sale	8 weeks
Missouri	Non-judicial	Trustee's Sale	8 weeks
Montana	Non-judicial	Trustee's Sale	6 months
Nebraska			
Mortgage	Judicial	Confirmation	7 months
Deed of Trust	Non-judicial	Sheriff's Sale	3 months
Nevada	Non-judicial	Trustee's Sale	130 days
New Hampshire	Non-judicial	Sale and Deed	4 months
New Jersey	Judicial	Sheriff's Sale	12 months
New Mexico	Judicial	Confirmation	20 weeks
New York:			
Allegany, Cattaraugus, Chautauqua, Erie, Genessee, Livingston, Monroe, Niagara, Ontario, Orleans, Steuben, Wyoming, Yates and Wayne Counties			
	Judicial	Referee's Sale	8 months
Other Counties	Judicial	Referee's Sale	9 months
North Carolina	Non-judicial	10 days after Sheriff's Sale	60 days
North Dakota	Judicial	Confirmation	18 weeks
Ohio:			
Cuyahoga County	Judicial	Confirmation	12 months
Other Counties	Judicial	Confirmation	9 months
Oklahoma	Judicial	Confirmation	8 months
Oregon	Non-judicial	Trustee's Sale	150 days
Pennsylvania:			
Western Counties under jurisdiction of the VA office in Pittsburgh			
	Judicial	Sheriff's Sale	6 months
Eastern Counties under jurisdiction of the VA office in Philadelphia			
	Judicial	Sheriff's Sale	8 months
Puerto Rico	Judicial	Confirmation	8 months
Rhode Island	Non-judicial	Sale and Deed	4 months
South Carolina	Judicial	Sale	9 months
South Dakota	Judicial	Sheriff's Sale	19 weeks
	Non-judicial	Sheriff's Sale	12 weeks
Tennessee	Non-judicial	Trustee's Sale	60 days
Texas	Non-judicial	Trustee's Sale	90 days*
*(First Tuesday of the month which is more than 60 and less than 90 days after referral)			
Utah	Non-judicial	Trustee's Sale	150 days
Vermont	Judicial	Certificate of Non-Redemption	12 months
Virginia	Non-judicial	Trustee's Sale	60 days
Washington	Non-judicial	Trustee's Sale	150 days
West Virginia	Non-judicial	Trustee's Sale	3 months
Wisconsin	Judicial	Confirmation	330 days
Wyoming	Non-judicial	Sheriff's Sale	90 days

TITLE 38 CFR 36.4300 SERIES
GUARANTY OR INSURANCE OF LOANS TO VETERANS

AUTHORITY: Sections 36.4300 through 36.4375 issued under 38 U.S.C. 501(a)

NOTE: Those requirements, conditions, or limitations which are expressly set forth in 38 U.S.C. chapter 37 are not restated in these regulations and must be taken into consideration in conjunction with §§36.4300 to 36.4393 of this part, inclusive.

SECTION.....PAGE

General Provisions

TITLE 38 CFR 36.4300 SERIES
GUARANTY OR INSURANCE OF LOANS TO VETERANS--Continued

SECTION **PAGE**

Underwriting Standards, Processing Procedures, and Lender Responsibility and Certification

TITLE 38 CFR 36.4300 SERIES
GUARANTY OR INSURANCE OF LOANS TO VETERANS

§36.4300 APPLICABILITY OF §§36.4300 TO 36.4393, INCLUSIVE

(a) Sections 36.4300 to 36.4393 of this part, inclusive, shall be applicable to each loan entitled to an automatic guaranty, or otherwise guaranteed or insured, on or after the date of publication in the *Federal Register*, and shall be applicable to such loans previously guaranteed or insured to the extent that no legal rights vested under the regulations are impaired.

(b) Title 38, U.S.C., chapter 37, is a continuation and restatement of the provisions of title III of the Servicemen's Readjustment Act of 1944, and may be considered an amendment to such Title III. References to the sections or chapters of Title 38, U.S.C., shall, where applicable, be deemed to refer to the prior corresponding provisions of the law. (Authority: 38 U.S.C. 501(a), 3703(c), 3712(g))

§36.4301 DEFINITIONS

Whenever used in 38 U.S.C., chapter 37 or §§36.4300 to 36.4375 of this part, inclusive, and §§36.4390 and 36.4393 of this part, unless the context otherwise requires, the terms defined in this section shall have the following meaning:

A period of more than 180 days. For the purposes of sections 3707 and 3702(a)(2)(C) of title 38, U.S.C., the term *a period of more than 180 days* shall mean 181 or more calendar days of continuous active duty.

Acquisition and improvement loan. A loan to purchase an existing property which includes additional funds for the purpose of installing energy conservation improvements or making other alterations, improvements, or repairs. (Authority: 38 U.S.C. 3703(c)(1), 3710(a)(1), (4), and (7))

Alterations. Any structural changes or additions to existing improved realty.

Automatic Lender. A lender that may process a loan or assumption without submitting the credit package to the Department of Veterans Affairs for underwriting review. Pursuant to 38 U.S.C. 3702(d) there are two categories of lenders who may process loans automatically: (1) Entities such as banks, savings and loan associations, and mortgage and loan companies that are subject to examination by an agency of the United States or any State and (2) lenders approved by the Department of Veterans Affairs pursuant to standards established by the Department of Veterans Affairs. (Authority: 38 U.S.C. 3702(d))

Condominium. Unless otherwise provided by State law, a condominium is a form of ownership where the buyer receives title to a three dimensional air space containing the individual living unit together with an undivided interest or share in the ownership of common elements.

Cost means the entire consideration paid or payable for or on account of the application of materials and labor to tangible property.

Credit Package. Any information, reports or verifications used by a lender, holder or authorized servicing agent to determine the creditworthiness of an applicant for a

Department of Veterans Affairs guaranteed loan or the assumer of such a loan. (Authority: 38 U.S.C. 3710 and 3714)

Date of First Uncured Default means the due date of the earliest payment not fully satisfied by the proper application of available credits or deposits.

Default means failure of a borrower to comply with the terms of a loan agreement.

Designated Appraiser means a person requested by the Secretary to render an estimate of the reasonable value of a property, or of a specified type of property, within a stated area for the purpose of justifying the extension of credit to an eligible veteran for any of the purposes stated in 38 U.S.C. Chapter 37. An appraiser on a fee basis is not an agent of the Secretary.

Discharge or Release. For purposes of basic eligibility a person will be considered discharged or released if the veteran was issued a discharge certificate under conditions other than dishonorable (38 U.S.C. 3702(c)). The term *discharge or release* includes (1) retirement from the active military, naval, or air service, and (2) the satisfactory completion of the period of active military, naval, or air service for which a person was obligated at the time of entry into such service in the case of a period who, due to enlistment or reenlistment, was not awarded a discharge or release from such period of service at the time of such completion thereof and who, at such time, would otherwise have been eligible for the award of a discharge or release under conditions other than dishonorable. (Authority: 38 U.S.C. 101(18))

Dwelling. Any building designed primarily for use as a home consisting of not more than four family units plus an added unit for each veteran if more than one eligible veteran participates in the ownership, except that in the case of a condominium housing development or project within the purview of 38 U.S.C. 3710(a)(6) and §§36.4356 through 36.4360(a) of this part the term is limited to a one single-family residential unit. Also, a manufactured home, permanently affixed to a lot owned by a veteran and classified as real property under the laws of the State where it is located. (Authority: 38 U.S.C. 3710(a)(9) and (f))

Economic Readjustment means rearrangement of an eligible veteran's indebtedness in a manner calculated to enable the veteran to meet obligations and thereby avoid imminent loss of the property which secures the delinquent obligation.

Energy Conservation Improvement. An improvement to an existing dwelling or farm residence through the installation of a solar heating system, a solar heating and cooling system, or a combined solar heating and cooling system, or through application of a residential energy conservation measure as prescribed in 38 U.S.C. 3710(d) or by the Secretary. (Authority: 38 U.S.C. 3710(a)(7))

Full Disbursement. Payment by a lender of the entire proceeds of a loan for the purposes described in the report of the lender in respect of such loan to the Secretary either:

(1) By payment to those contracting with the borrower for such purposes, or

(2) By payment to the borrower, or

(3) By transfer to an account against which the borrower can draw at will, or

(4) By transfer to an escrow account, or

(5) By transfer to an earmarked account if

(i) The amount is not in excess of 10 percent of the loan, or

(ii) The loan is an acquisition and improvement loan pursuant to §36.4301, or

(iii) The loan is one submitted by a lender of the class specified in 38 U.S.C. 3702(d) or 3703(a)(2). (Authority: 38 U.S.C. 3703(c)(1))

Graduated Payment Mortgage Loan. A loan for the purpose of acquiring a single-family dwelling unit involving a plan for repayment in which a portion of the interest due is deferred for a period of time. The interest so deferred is added to the principal balance thus resulting in a principal amount greater than at loan origination (negative amortization). The monthly payments increase on an annual basis (graduate) for a predetermined period of time until the payments reach a level which will fully amortize the loan during the remaining loan term. (Authority: 38 U.S.C. 3703(c) and (d))

Guaranty. The obligation of the United States, assumed by virtue of 38 U.S.C. Chapter 37, to repay a specified percentage of a loan upon the default of the primary debtor.

Holder. The lender or any subsequent assignee or transferee of the guaranteed or insured obligation or the authorized servicing agent of the lender or of the assignee or transferee if the obligation has been assigned or transferred.

Home means place of residence.

Improvements. Any alteration that improves the property for the purpose for which it is occupied.

Indebtedness. The unpaid principal and interest plus any other amounts allowable under the terms of a loan including those authorized by statute and consistent with §§36.4300 to 36.4393 of this part, inclusive, which have been paid and debited to the loan account as of the applicable date established pursuant to paragraph (f) of §36.4319 or §36.4321 of this part. (Authority: 38 U.S.C. 3732)

Insurance means the obligation assumed by the United States to indemnify a lender to the extent specified in §§36.4300 to 36.4393, inclusive, for any loss incurred upon any loan insured under 38 U.S.C. 3703(a)(2).

Insurance Account means the record of the amount available to a lender or purchaser for losses incurred on loans insured under 38 U.S.C. 3715.

Lender. The payee or assignee or transferee of an obligation at the time it is guaranteed or insured. This term also includes any sole proprietorship, partnership, or corporation and the owners, officers, and employees of a sole proprietorship, partnership, or corporation engaged in the origination, procurement, transfer, servicing, or funding or a loan which is guaranteed or insured by VA. (Authority: 38 U.S.C. 3704(d); 3712(g))

Lien means any interest in, or power over, real or personal property, reserved by the vendor, or created by the parties or by operation of law, chiefly or solely for the purpose of assuring the payment of the purchase price, or a debt, and irrespective of the identity

of the party in whom title to the property is vested, including but not limited to mortgages, deeds with a defeasance therein or collaterally, deeds of trust, security deeds, mechanics' liens, lease-purchase contracts, conditional sales contracts, consignments.

Liquidation Sale. Any judicial, contractual or statutory disposition of real property, under the terms of the loan instruments and applicable law, to liquidate a defaulted loan that is secured by such property. This includes a voluntary conveyance made to avoid such disposition of the obligation or of the security. (Authority: 38 U.S.C. 3732)

Lot. A parcel of land acceptable to the Secretary as a manufactured home site. (Authority: 38 U.S.C. 3710(a)(9))

Manufactured Home. A moveable dwelling unit designed and constructed for year-round occupancy by a single family, on land, containing permanent eating, cooking, sleeping and sanitary facilities. A double-wide manufactured home is a moveable dwelling designed for occupancy by one family and consisting of (1) two or more units intended to be joined together horizontally when located on a site, but capable of independent movement or (2) a unit having a section or sections which unfold along the entire length of the unit. For the purposes of this section of VA regulations, manufactured home/lot loans guaranteed under the purview of §§36.4300 to 36.4393, inclusive, must be for units permanently affixed to a lot and considered to be real property under the laws of the State where it is located. If the loan is for the purchase of a manufactured home and lot it must be considered as one loan. (Authority: 38 U.S.C. 3710(a)(9))

Net Loss (insured loans) means the indebtedness, plus any other charges authorized under §36.4313, remaining unsatisfied after the liquidation of all available security and recourse to all intangible rights of the holder against those obligated on the debt.

Net Value. The fair market value of real property, minus the total of the costs the Secretary estimates would be incurred by VA resulting from the acquisition and disposition of the property for property taxes, assessments, liens, property maintenance, property improvement, administration, and resale. For purposes of determination of net value, *property improvement* is defined as any repair which must be completed to satisfy minimum property requirements for existing construction as described by the Secretary. Costs other than property improvement will be estimated as a percentage of the fair market value. Each year VA will review the average operating expenses incurred for properties acquired under §36.4320 of this part which were sold during the preceding 3 fiscal years and the average administrative cost to the government associated with the property management activity. The cost items reviewed will be:

(1) **Property Operating Expenses**. All disbursements made for payment of taxes, assessments, liens, property maintenance and related repairs, management broker's fees and commissions, and any other charges to the property account excluding property improvements and selling expenses.

(2) **Selling Expenses**. All disbursements for sales commissions plus any other costs incurred and paid in connection with the sale of the property.

(3) **Administrative Costs**. An estimate of the total costs for VA of personnel compensation and overhead (including all travel, transportation, standard level user charges (SLUC), communication, utilities, printing, supplies, equipment, insurance claims and other services) associated with the acquisition, management and disposition of

property acquired under §36.4320 of this part. The average administrative costs will be determined by:

(i) Dividing the salary and benefits cost by the average number of properties on hand and adjusting this figure based on the average holding time for properties sold during the preceding fiscal year; then

(ii) Dividing part (i) by the VBA ratio of personal services to total obligations.

The three cost averages will be added and the sum will be divided by the average fair market value at the time of acquisition for properties which were sold during the 3 preceding fiscal years to derive the percentage to be used in estimating net value. (The Secretary may, when determining property management costs, group properties in incremental value brackets.) The calculation of net value will be based on the actual cost incurred over the last 3 years. Based on fiscal year 1989 data, the percentage to be used when calculating net value will be 11.45 percent. The fiscal year and the percentage will be updated annually through a notice in the *Federal Register*. (Authority: 38 U.S.C. 3732)

Purchase Price. The entire legal consideration paid or payable upon or on account of the sale of property, exclusive of acquisition costs, or for the cost of materials and labor to be applied to the property.

Real Estate Loan. Any obligation incurred for the purchase of real property or a leasehold estate as limited in §§36.4300 to 36.4393, inclusive, or for the construction of fixtures or appurtenances thereon or for alterations, improvements, or repairs thereon required by §§36.4300 to 36.4393, inclusive, to be secured by a lien on such property or is so secured. Loans for the purpose specified in 38 U.S.C. 3710(a)(5) (refinancing of mortgage loans or other liens on a dwelling or farm residence), loan for the purpose specified in 38 U.S.C. 3710(a)(8) (refinancing of a VA guaranteed, insured or direct loan to lower the interest rate) loans for the purposes specified in 38 U.S.C. 3710(a)(9) (purchase of manufactured homes/lots or the refinancing of such loans, in order to reduce the interest rate or purchase a lot, in States in which manufactured homes, when permanently affixed to a lot, are considered real property, and loans to purchase one-family residential units in condominium housing developments or projects within the purview of 38 U.S.C. 3710(a)(6) and §§36.4356 through 36.4360a shall also be considered real estate loans.

Reasonable Value means that figure which represents the amount a reputable and qualified appraiser, unaffected by personal interest, bias, or prejudice, would recommend to a prospective purchaser as a proper price or cost in the light of prevailing conditions.

Registered Mail. The term *registered mail* wherever used in the regulations concerning guaranty or insurance of loans to veterans shall include certified mail.

Repairs. Any alteration of existing improved realty or equipment which is necessary or advisable for protective, safety or restorative purposes.

Repossession - Repossessed means recovery or acquisition of such physical control of property (pursuant to the provisions of the security instrument or as otherwise provided by law) as to make further legal or other action unnecessary in order to obtain actual possession of the property or to dispose of the same by sale or otherwise.

Residential Property (1) Any one-family residential unit in a condominium housing development within the purview of 38 U.S.C. 3710(a)(6) and §§36.4356 through 36.4360a; (2) any manufactured home permanently affixed to a lot owned or being purchased by a veteran and considered to be real property under the laws of the State where it is located; and (3) any improved real property (other than a condominium housing development or a manufactured home and/or lot) or leasehold estate therein as limited by §§36.4300 to 36.4393, inclusive, the primary use of which is for occupancy as a home, consisting of not more than four family units, plus an added unit for each eligible veteran if more than one participates in the ownership thereof, or (4) any land to be purchased out of the proceeds of a loan for the construction of a dwelling, and on which such dwelling is to be erected. (Authority: 38 U.S.C. 3710(f)(2) and (3))

Secretary. The Secretary of Veterans Affairs, or any employee of VA authorized to act in the Secretary's stead.

Servicing Agent. An agent designated by the loan holder as the entity to collect installments on the loan and/or perform other functions as necessary to protect the interests of the holder. (Authority: 38 U.S.C. 3714)

Specified Amount. A sum, equal to the lesser of the net value of real property or the total indebtedness secured thereby, which the Secretary designates as the minimum amount to be credited to the indebtedness incident to a liquidation sale. (Authority: 38 U.S.C. 3732)

Unguaranteed Portion of the Indebtedness. The indebtedness computed as of the applicable date of under paragraph (f) of §36.4319 or §36.4321 of this part minus the amount of the guaranty payable as of such date. (Authority: 38 U.S.C. 3732) (Authority: 38 U.S.C. 501(a), 3703(c)(1))

GENERAL PROVISIONS

§36.4302 COMPUTATION OF GUARANTIES OR INSURANCE CREDITS

(a) With respect to a loan to a veteran guaranteed under 38 U.S.C. 3710 the guaranty shall not exceed the lesser of the dollar amount of entitlement available to the veteran; or

(1) 50 percent of the original principal loan amount where the loan amount is not more than $45,000; or

(2) $22,500 where the original principal loan exceeds $45,000, but is not more than $56,250; or

(3) Except as provided in subparagraph (4), the lesser of $36,000 or 40 percent of the original principal loan amount where the loan amount exceeds $56,250; or

(4) The lesser of $46,000 or 25 percent of the original principal loan amount where the loan amount exceeds $144,000 and the loan is for the purchase or construction of a home or the purchase of a condominium unit. (Authority: 38 U.S.C. 3703(a))

(b) With respect to a loan guaranteed under 38 U.S.C. 3710(a)(8) or (9)(B)(i) the dollar amount of guaranty may not exceed the original dollar amount of guaranty on the loan being refinanced. (Authority: 38 U.S.C. 3703(a))

(c) An amount equal to 15 percent of the original principal amount of each insured loan shall be credited to the insurance account of the lender and shall be charged against the guaranty entitlement of the borrower: *Provided*, That no loan may be insured unless the borrower has sufficient entitlement remaining to permit such credit.

(d) Subject to the provisions of paragraph (g) of §36.4303, the following formulas shall govern the computation of the amount of the guaranty or insurance entitlement which remains available to an eligible veteran after prior use of entitlement:

(1) If a veteran previously secured a nonrealty (business) loan, the amount of nonrealty entitlement used is doubled and subtracted from $36,000. The sum remaining is the amount of available entitlement for use except that (i) entitlement may be increased by up to $10,000 if the loan amount exceeds $144,000 and the loan is for purchase or construction of a home or purchase of a condominium, and (ii) entitlement for manufactured home loans that are to be guaranteed under 38 U.S.C. 3712 may not exceed $20,000.

(2) If a veteran previously secured a realty (home) loan, the amount of realty (home) loan entitlement used is subtracted from $36,000. The sum remaining is the amount of available entitlement for use except that (i) entitlement may be increased by up to $10,000 if the loan amount exceeds $144,000 and the loan is for purchase or construction of a home or purchase of a condominium, and (ii) entitlement for manufactured home loans that are to be guaranteed under 38 U.S.C. 3712 may not exceed $20,000.

(3) If a veteran previously secured a manufactured home loan under 38 U.S.C. 3712; the amount of entitlement used for that loan is subtracted from $36,000. The sum remaining is the amount of available entitlement for home loans or manufactured home/lot loans guaranteed under 38 U.S.C. 3710, except that entitlement may be increased by up to $10,000 if the loan amount exceeds $144,000 and the loan is for

purchase or construction of a home or purchase of a condominium. To determine the amount of entitlement available for manufactured home loans, processed under 38 U.S.C. 3712, the amount of entitlement previously used for that purpose is subtracted from $20,000. The sum remaining is the amount of available entitlement for use for manufactured home loan purposes under 38 U.S.C. 3712. (Authority: 38 U.S.C. 3703(a), 3712(c)(4))

(e) For the purpose of computing the remaining guaranty or insurance benefit to which a veteran is entitled, loans guaranteed prior to the effective date of §§36.4300 to 36.4393, inclusive, shall be taken into consideration as if made subsequent thereto.

(f) A loan eligible for insurance may be either guaranteed or insured at the option of the borrower and the lender: Provided, That if the Secretary is not advised of the exercise of such option at the time the loan is reported pursuant to §36.4303, such loan will not be eligible for insurance.

(g) A guaranty is reduced or increased pro rata with any deduction or increase in the amount of the guaranteed indebtedness, but in no event will the amount payable on a guaranty exceed the amount of the original guaranty or the percentage of the indebtedness corresponding to that of the original guaranty whichever is less. However, on a graduated payment mortgage loan, the percentage of guaranty applicable to the original loan amount pursuant to paragraph (a) of this section shall apply to the loan indebtedness to the extent scheduled deferred interest is added to principal during the graduation period without regard to the original maximum dollar amount of guaranty. (Authority: 38 U.S.C. 3703(b) and (d))

(h) The amount of any guaranty or the amount credited to a lender's insurance account in relation to any insured loan shall be charged against the original or remainder of the guaranty benefit of the borrower. Complete or partial liquidation, by payment or otherwise, of the veteran's guaranteed or insured indebtedness does not increase the remainder of the guaranty benefit, if any, otherwise available to the veteran. When the maximum amount of guaranty or insurance legally available to a veteran shall have been granted, no further guaranty or insurance is available to the veteran.

(i) Notwithstanding the provisions of paragraph (g) of this section, the Secretary may exclude the amount of guaranty or insurance entitlement used for any guaranteed or insured loan provided:

(1) The property which served as security for the loan has been disposed of by the veteran, or has been destroyed by fire or other natural hazard; and

(2) The loan has been repaid in full, or the Secretary has been released from liability as to the loan, or if the Secretary has suffered a loss on said loan, such loss has been paid in full; or

(3) A veteran-transferee has agreed to assume the outstanding balance on the loan and consented to the use of his or her entitlement to the extent the entitlement of the veteran-transferor has been used originally.

(4) The loan has been repaid in full, and the loan for which the veteran seeks to use entitlement is secured by the same property which secured the fully repaid loan. (Authority: 38 U.S.C. 3710(e)(3))

(j) (1) The amount of guaranty entitlement, available and unused, of an eligible unmarried surviving spouse (whose eligibility does not result from his or her own service) is determinable in the same manner as in the case of any veteran, and any entitlement which the decedent (who was his or her spouse) used shall be disregarded. A certificate as to the eligibility of such surviving spouse, issued by the Secretary, shall be a condition precedent to the guaranty or insurance of any loan made to a surviving spouse in such capacity. (Authority: 38 U.S.C. 3701(a))

(2) An unmarried surviving spouse who was a co-obligor under an existing VA guaranteed, insured or direct loan shall be considered to be a veteran eligible for an interest rate reduction refinancing loan pursuant to 38 U.S.C. 3710(a)(8) or (9)(B)(i). (Authority: 38 U.S.C. 3710(e)(3)) (Authority: 38 U.S.C. 501(a), 3703(c)(1))

§36.4303 REPORTING REQUIREMENTS

(a) With respect to loans automatically guaranteed under 38 U.S.C. 3703(a)(1) evidence of the guaranty will be issuable to a lender of a class described under 38 U.S.C. 3702(d) if the loan is reported to the Secretary within 60 days following full disbursement, and upon the certification of the lender that:

(1) No default exists thereunder which has continued for more than 30 days;

(2) Except for acquisition and improvement loans as defined in §36.4301, any construction, repairs, alterations, or improvements effected subsequent to the appraisal of reasonable value, and paid for out of the proceeds of the loan, which have not been inspected and approved upon completion by a compliance inspector designated by the Secretary have been completed properly in full accordance with the plans and specifications upon which the original appraisal was based, and any deviations or changes of identity in said property have been approved as required in §36.4304 concerning guaranty or insurance of loans to veterans;

(3) The loan conforms otherwise with the applicable provisions of 38 U.S.C., Chapter 37 and of the regulations concerning guaranty or insurance of loans to veterans. (Authority: 38 U.S.C. 3703(c)(1))

(b) Loans made pursuant to 38 U.S.C. 3715 although not entitled to automatic insurance thereunder may, when made by a lender of a class described in 38 U.S.C. 3702(d)(1), be reported for issuance of an insurance credit. (Authority: 38 U.S.C. 3702(d), 3715)

(c) Each loan proposed to be made to an eligible veteran by a lender not within a class described in 38 U.S.C. 3702(d) shall be submitted to the Secretary for approval prior to closing. Lenders described in 38 U.S.C. 3702(d) shall have the optional right to submit any loan for such prior approval. The Secretary upon determining any loan so submitted to be eligible for a guaranty, or for insurance, will issue a certificate of commitment with respect thereto.

(d) A certificate of commitment shall entitle the holder to the issuance of the evidence of guaranty or insurance upon the ultimate actual payment of the full proceeds of the loan for the purposes described in the original report and upon the submission within 60 days thereafter of a supplemental report showing that fact and:

(1) The identity of any property purchased therewith,

(2) That all property purchased or acquired with the proceeds of the loan has been encumbered as required by the regulations concerning guaranty or insurance of loans to veterans,

(3) Except for acquisition and improvement loans as defined in §36.4301, any construction, repairs, alterations, or improvements paid for out of the proceeds of the loan which have not been inspected and approved subsequent to completion by a compliance inspector designated by the Secretary have been completed properly in full accordance with the plans and specifications upon which the original appraisal was based and that any deviations or changes of identity in said property have been approved as required by §36.4304; and

(4) That the loan conforms otherwise with the applicable provisions of 38 U.S.C. Chapter 37 and the regulations concerning guaranty or insurance of loans to veterans. (Authority: 38 U.S.C. 3703(c)(1))

(e) Upon the failure of the lender to report in accordance with the provisions of paragraph (d) of this section, the certificate of commitment shall have no further effect, or the amount of guaranty or insurance shall be reduced pro rata, as may be appropriate under the facts of the case: *Provided, nevertheless*, That if the loan otherwise meets the requirements of this section, said certificate of commitment may be given effect by the Secretary notwithstanding the report is received after the date otherwise required.

(f) Evidence of a guaranty will be issued by the Secretary by appropriate endorsement on the note or other instrument evidencing the obligation, or by a separate certificate at the option of the lender. Notice of credit to an insurance account will be given to the lender. Unused certificates of eligibility issued prior to March 1, 1946, are void. No certificate of commitment shall be issued and no loan shall be guaranteed or insured unless the lender, the veteran, and the loan are shown to be eligible. Evidence of guaranty or insurance will not be issued on any loan for the purchase or construction of residential property unless the veteran, or the veteran's spouse in the case of a veteran who cannot occupy the property because of active duty status with the Armed Forces, certifies in such form as the Secretary shall prescribe, that the veteran, or spouse of the active duty veteran, intends to occupy the property as his or her home. Guaranty or insurance evidence will not be issued on any loan for the alteration, improvement, or repair of any residential property or on a refinancing loan unless the veteran, or spouse of an active duty service member, certifies that he or she presently occupies the property as his or her home. An exception to this is if the home improvement or refinancing loan is for extensive changes to the property which will prevent the veteran or the spouse of the active duty veteran from occupying the property while the work is being completed. In such case the veteran or spouse of the active duty veteran must certify that he or she intends to occupy or to reoccupy the property as his or her home upon completion of the substantial improvements or repairs. All of the mentioned certifications must take place at the time of loan application and closing except in the case of loans automatically guaranteed, in which case veterans or in the case of an active duty veteran, the veteran's spouse shall make the required certifications only at the time the loan is closed. (Authority: 38 U.S.C. 3704(c))

(g) Subject to compliance with the regulations concerning guaranty or insurance of loans to veterans, the certificate of guaranty or the evidence of insurance credit will be issuable within the available entitlement of the veteran on the basis of the loan stated in the final loan report or certification of loan disbursement, except for refinancing loans for interest rate reductions. The available entitlement of a veteran will be determined by the Secretary as of the date of receipt of an application for guaranty or insurance of a loan or

of a loan report. Such date of receipt shall be the date the application or loan report is date stamped into the Department of Veterans Affairs. Eligibility derived from the most recent period of service.

(1) Shall cancel any unused entitlement derived from any earlier period of service, and

(2) Shall be reduced by the amount by which entitlement from service during any earlier period has been used to obtain a direct, guaranteed, or insured loan.

(i) On property which the veteran owns at the time of application, or

(ii) As to which the Secretary has incurred actual liability or loss, unless in the event of loss or the incurrence and payment of such liability by the Secretary the resulting indebtedness of the veteran to the United States has been paid in full.

Provided, That if the Secretary issues or has issued a certificate of commitment covering the loan described in the application for guaranty or insurance or in the loan report, the amount and percentage of guaranty or the amount of the insurance credit contemplated by the certificate of commitment shall not be subject to reduction if the loan has been or is closed on a date which is not later than the expiration date of the certificate of commitment, notwithstanding that the Secretary in the meantime and prior to the issuance of the evidence of guaranty or insurance shall have incurred actual liability or loss on a direct, guaranteed, or insured loan previously obtained by the borrower. For the purposes of this paragraph, the Secretary will be deemed to have incurred actual loss on a guaranteed or insured loan if the Secretary has paid a guaranty or insurance claim thereon and the veteran's resultant indebtedness to the Government has not been paid in full, and to have incurred actual liability on a guaranteed or insured loan if the Secretary is in receipt of a claim on the guaranty or insurance or is in receipt of a notice of default. In the case of a direct loan, the Secretary will be deemed to have incurred an actual loss if the loan is in default. A loan, the proceeds of which are to be disbursed progressively or at intervals, will be deemed to have been closed for the purposes of this paragraph if the loan has been completed in all respects excepting the actual "pay-out" of the entire loan proceeds. (Authority: 38 U.S.C. 3702(a), 3710(c))

(h) Any amounts which are disbursed for an ineligible purpose shall be excluded in computing the amount of guaranty or insurance credit.

(i) Notwithstanding the lender has erroneously, but without intent to misrepresent, made certification with respect to paragraph (a)(1) of this section, the guaranty or insurance will become effective upon the curing of such default and its continuing current for a period of not less than 60 days thereafter. For the purpose of this paragraph a loan will be deemed current so long as the installment is received within 30 days after its due date.

(j) No guaranty or insurance commitment or evidence of guaranty or insurance will be issuable in respect to any loan to finance a contract which:

(1) Is for the purchase, construction, repair, alteration, or improvement of a dwelling or farm residence;

(2) Is dated on or after June 4, 1969;

(3) Provides for a purchase price or cost to the veteran in excess of the reasonable value established by the Secretary; and

(4) Was signed by the veteran prior to the veteran's receipt of notice of such reasonable value; unless such contract includes, or is amended to include, a provision substantially as follows:

> It is expressly agreed that, notwithstanding any other provisions of this contract, the purchaser shall not incur any penalty by forfeiture of earnest money or otherwise or be obligated to complete the purchase of the property described herein, if the contract purchase price or cost exceeds the reasonable value of the property established by the Department of Veterans Affairs. The purchaser shall, however, have the privilege and option of proceeding with the consummation of this contract without regard to the amount of the reasonable value established by the Department of Veterans Affairs.
> (Authority: 38 U.S.C. 501(a), 3703(c)(1))

(k) With respect to any loan for which a commitment was made on or after March 1, 1988, the Secretary must be notified whenever the holder receives knowledge of disposition of the residential property securing a Department of Veterans Affairs guaranteed loan.

(1) If the seller applies for prior approval of the assumption of the loan, then:

(i) A holder (or its authorized servicing agent) who is an automatic lender must examine the creditworthiness of the purchaser and determine compliance with the provisions of 38 U.S.C. 3714. The creditworthiness review must be performed by the party that has automatic authority. If both the holder and its servicing agent are automatic lenders, then they must decide between themselves which one will make the determination of creditworthiness, whether the loan is current and whether there is a contractual obligation to assume the loan, as required by 38 U.S.C. 3714. If the actual loan holder does not have automatic authority and its servicing agent is an automatic lender, then the servicing agent must make the determinations required by 38 U.S.C. 3714 on behalf of the holder. The actual holder will remain ultimately responsible for any failure of its servicing agent to comply with the applicable law and Department of Veterans Affairs regulations.

(A) If the assumption is approved and the transfer of the security is completed, then the notice required by this paragraph shall consist of the credit package (unless previously provided in accordance with paragraph (k)(1)(i)(B) of this section) and a copy of the executed deed and/or assumption agreement as required by the Department of Veterans Affairs office of jurisdiction. The notice shall be submitted to the Department of Veterans Affairs with the Department of Veterans Affairs receipt for the funding fee provided for in §36.4312(e)(3) of this part.

(B) If the application for assumption is disapproved, the holder shall notify the seller and the purchaser that the decision may be appealed to the Department of Veterans Affairs office of jurisdiction with 30 days. The holder shall make available to that Department of Veterans Affairs office all items used by the holder in making the holder's decision in case the decision is appealed to the Department of Veterans Affairs. If the application remains disapproved after 60 days (to allow time for appeal to and review by the Department of Veterans Affairs) then the holder must refund $50 of any fee previously collected under the provisions of §36.4312(d)(8) of this part. If the

application is subsequently approved and the sale is completed, then the holder (or its authorized servicing agent) shall provide the notice described in paragraph (k)(1)(i)(A) of this section.

(C) In performing the requirements of paragraphs (k)(1)(i)(A) or (k)(1)(i)(B) of this section the holder must complete its examination of the creditworthiness of the prospective purchaser and advise the seller no later than 45 days after the date of receipt by the holder of a complete application package for the approval of the assumption. The 45-day period may be extended by an interval not to exceed the time caused by delays in processing of the application which are documented as beyond the control of the holder, such as employers or dispositories not responding to requests for verifications, which were timely forwarded, or followups on those requests.

(ii) If neither the holder nor its authorized servicing agent is an automatic lender, the notice to the Department of Veterans Affairs shall include:

(A) Advice regarding whether the loan is current or in default;

(B) A copy of the purchase contract; and

(C) A complete credit package developed by the holder which the Secretary may use for determining the creditworthiness of the purchaser.

(D) The notice and documents required by this section must be submitted to the Department of Veterans Affairs office of jurisdiction no later than 35 days after the date of receipt by the holder of a complete application package for the approval of the assumption, subject to the same extensions as provided in paragraph (k)(1)(i) of this section. If the assumption is not automatically approved by the holder or its authorized agent, pursuant to the automatic authority provisions, $50 of any fee collected in accordance with §36.4312(d)(8) of this part must be refunded. If the Department of Veterans Affairs does not approve the assumption, the holder will be notified and an additional $50 of any fee collected under §36.4312(d)(8) of this section must be refunded following the expiration of the 30-day appeal period set out in paragraph (k)(1)(i)(B) of this section. If such an appeal is made to the Department of Veterans Affairs, then the review will be conducted at the Department of Veterans Affairs office of jurisdiction by an individual who was not involved in the original disapproval decision. If the application for assumption is approved and the transfer of security is completed, then the holder (or its authorized servicing agent) shall provide the notice required in paragraph (k)(1)(i)(A) of this section.

(2) If the seller fails to notify the holder before disposing of property securing the loan, the holder shall notify the Secretary within 60 days after learning of the transfer. Such notice shall advise whether or not the holder intends to exercise its option to immediately accelerate the loan and whether or not an opportunity will be extended to the transferor and transferee to apply for retroactive approval of the assumption under the terms of this paragraph. (Authority: 38 U.S.C. 3714)

§36.4304 DEVIATIONS, CHANGES OF IDENTITY

A deviation of more than 5 percent between the estimates upon which a certificate of commitment has been issued and the report of final payment of the proceeds of the loan, or a change in the identity of the property upon which the original appraisal was based, will invalidate the certificate of commitment unless such deviation or change be approved by the Secretary. Any deviation in excess of 5 percent or change in the identity

of the property upon which the original appraisal was based must be supported by a new or supplemental appraisal of reasonable value: *Provided*, That substitution of materials of equal or better quality and value approved by the veteran and the designated appraiser shall not be deemed a *change in the identity of the property* within the purview of this section. A deviation not in excess of 5 percent will not require the prior approval of the Secretary.

§36.4305 PARTIAL DISBURSEMENT

In cases where intervening circumstances make it impracticable to complete the actual paying out of the loan originally proposed, or justify the lender in declining to make further disbursements on a construction loan, evidence of guaranty or of insurance of the loan or the proper pro rata part thereof will be issuable if the loan is otherwise eligible for automatic guaranty or a certificate of commitment was issued thereon, *Provided*:

(a) A report of the loan is submitted to the Secretary within a reasonable time subsequent to the last disbursement, but in no event more than 90 days thereafter, unless report of the facts and circumstances is made and an extension of time obtained from the Secretary.

(b) There has been no default on the loan, except that the existence of a default shall not preclude issuance of a guaranty certificate or insurance advice if a certificate of commitment was issued with respect to the loan.

(c) The Secretary determines that a person of reasonable prudence similarly situated would not make further disbursements in the situation presented.

(d) There has been full compliance with the provisions of 38 U.S.C. Chapter 37 and of the applicable regulations up to the time of the last disbursement.

(e) In the case of a construction loan when the construction is not fully completed, the amount and percentage of the guaranty and the amount of the loan for the purposes of insurance or accounting to the Secretary shall be based upon such portion of the amount disbursed out of the proceeds of the loan which, when added to any other payments made by or on behalf of the veteran to the builder or the contractor, does not exceed 80 percent of the value of that portion of the construction performed (basing value on the contract price) plus the sum, if any, disbursed by the lender out of the proceeds of the loan for the land on which the construction is situated: *And provided further*, That the lender shall certify as follows:

(1) Any amount advanced for land is protected by title or lien as provided in the regulations concerning guaranty or insurance of loans to veterans; and

(2) No enforceable liens, for any work done or material furnished for that part of the construction completed and for which payment has been made out of the proceeds of the loan, exist or can come into existence.

§36.4306 REFINANCING OF MORTGAGE OR OTHER LIEN INDEBTEDNESS

(a) Any loan for the purpose of refinancing (38 U.S.C. 3710(a)(5)) an existing mortgage loan or other indebtedness secured by a lien of record on a dwelling or farm residence owned and occupied or to be reoccupied if the refinancing loan is for the completion of major alterations, repairs, or improvements to the property, by an eligible

veteran as the veteran's home, or in the case of an eligible veteran unable to occupy the property because of active duty status in the Armed Forces, occupied or to be reoccupied by the veteran's spouse as the spouse's home, shall be eligible for guaranty in an amount as computed under §36.4302(a) provided that:

(1) The amount of the loan may not exceed an amount equal to 90 percent of the reasonable value of the dwelling or farm residence which will secure the loan, as determined by the Secretary. (Authority: 38 U.S.C. 3710(e)(1) and 3710(h))

(2) The dollar amount of discount, if any, to be paid by the veteran is reasonable in amount as determined by the Secretary in accordance with §36.4312(d)(7)(i),

(3) The loan is otherwise eligible for guaranty.

(b) Reserved.

(c) Nothing shall preclude guaranty of a loan to an eligible veteran having home loan guaranty entitlement to refinance under the provisions of 38 U.S.C. 3710(a)(5) a VA guaranteed or insured (or direct) mortgage loan made to him or her which is outstanding on the dwelling or farm residence owned and occupied or to be reoccupied after the completion of major alterations, repairs, or improvements to the property, by the veteran as a home, or in the case of an eligible veteran unable to occupy the property because of active duty status in the Armed Forces, occupied or to be reoccupied by the veteran's spouse as the spouse's home. (Authority: 38 U.S.C. 3710(e)(1))

(d) A refinancing loan may include contractual prepayment penalties, if any, due the holder of the mortgage or other lien indebtedness to be refinanced.

(e) Reserved.

(f) Nothing in this section shall preclude the refinancing of the balance due for the purchase of land on which new construction is to be financed through the proceeds of the loan, or the refinancing of the balance due on an existing land sale contract relating to a veteran's dwelling or farm residence.

(g) A veteran may refinance (38 U.S.C. 3710(a)(9)(B)(ii)) an existing loan that was for the purchase of, and is secured by, a manufactured home in order to purchase the lot on which the manufactured home is or will be permanently affixed, provided the following requirements are met:

(1) The refinancing of a manufactured home and the purchase of a lot must be considered as one loan;

(2) The manufactured home upon being permanently affixed to the lot will be considered real property under the laws of the State where it is located;

(3) The loan must be secured by the same manufactured home which is being refinanced and the real property on which the manufactured home is or will be located;

(4) The amount of the loan may not exceed an amount equal to the sum of the balance of the loan being refinanced; the purchase price, not to exceed the reasonable value of the lot; the costs of the necessary site preparation of the lot as determined by the Secretary; a reasonable discount as authorized in §36.4312(d)(6) with respect to that

portion of the loan used to refinance the existing purchase money lien on the manufactured home, and closing costs as authorized in §36.4312.

(5) If the loan being refinanced was guaranteed by VA, the portion of the loan made for the purpose of refinancing an existing purchase money manufactured home loan may be guaranteed without regard to the outstanding guaranty entitlement available for use by the veteran, and the veteran's guaranty entitlement shall not be charged as a result of any guaranty provided for the refinancing portion of the loan. For the purposes enumerated in 38 U.S.C. 3702(b) the refinancing portion of the loan shall be considered to have been obtained with the guaranty entitlement used to obtain the VA-guaranteed loan being refinanced. The total guaranty for the new loan shall be the sum of the guaranty entitlement used to obtain VA-guaranteed loan being refinanced and any additional guaranty entitlement available to the veteran. However, the total guaranty may not exceed the guaranty amount as calculated under §36.4302(a) of this part. (Authority: 38 U.S.C. 3703(a))

§36.4306a INTEREST RATE REDUCTION REFINANCING LOAN

(a) Pursuant to 38 U.S.C. 3710(a)(8) and (9)(B)(i), a veteran may refinance an existing VA guaranteed, insured or direct loan to reduce the interest rate payable on the existing loan provided the following requirements are met:

(1) The loan must be secured by the same dwelling or farm residence as the loan being refinanced; and

(2) The veteran must own the dwelling or farm residence securing the loan; and

(i) Must occupy the dwelling or residence as his or her home; or

(ii) Must have previously occupied the dwelling or residence as his or her home and must certify, in such form as the Secretary shall require, that he or she has previously occupied the dwelling or residence; or

(iii) In any case in which the veteran is on, or was on, active duty status as a member of the Armed Forces and is unable, or was unable, to occupy the residence or dwelling as a home because of such active duty status, the spouse of the veteran must occupy, or must have previously occupied, such dwelling or residence as the spouse's home and must certify to that occupancy in such form as the Secretary shall require. (Authority: 38 U.S.C. 3710(e)(1))

(3) The amount of the refinancing loan may not exceed an amount equal to the sum of the balance of the loan being refinanced and such closing costs as authorized by §36.4312(d) and a discount not to exceed a dollar amount determined in accordance with §36.4312(d)(7)(i);

(4) The dollar amount of the guaranty of the 38 U.S.C. 3710(a)(8) or (9)(B)(i) loan may not exceed the original dollar amount of guaranty applicable to the loan being refinanced, less any dollar amount of guaranty previously paid as a claim on the loan being refinanced; and

(5) The term of the refinancing loan (38 U.S.C. 3710(a)(8)) may not exceed the original term of the loan being financed plus ten years or the maximum loan term allowed under 38 U.S.C. 3703(d)(1), whichever is less. For manufactured home loans that were previously guaranteed under 38 U.S.C. 3712 the loan term, if being refinanced under 38

U.S.C. 3710(a)(9)(B)(i), may exceed the original term of the loan but may not exceed the maximum loan term allowed under 38 U.S.C. 3703(d)(1). (Authority: 38 U.S.C. 3710(e)(1))

(b) Notwithstanding any other regulatory provision, the interest rate reduction refinancing loan may be guaranteed without regard to the amount of guaranty entitlement available for use by the veteran and the amount of the veteran's remaining guaranty entitlement, if any, shall not be charged for an interest rate reduction refinancing loan. The interest rate reduction refinancing loan will be guaranteed with the lesser of the entitlement used by the veteran to obtain the loan being refinanced or the amount of the guaranty as calculated under §36.4302(a) of this part. The veteran's loan guaranty entitlement originally used for the purpose as enumerated in 38 U.S.C. 3710(a)(1) through (7) and (9)(A)(i) and (ii) and subsequently transferred to an interest rate reduction refinancing loan (38 U.S.C. 3710(a)(8) or (9)(B)(i)) shall be eligible for restoration when the interest rate reduction refinancing loan or subsequent interest rate reduction refinancing loans on the same property meets the requirements of §36.4302(h). (Authority: 38 U.S.C. 3703(a))

(c) Title to the estate which is refinanced for the purpose of an interest rate reduction must be in conformity with §36.4350. (Authority: 38 U.S.C. 3710(a)(8), (9)(B)(i) and (e))

§36.4307 JOINT LOANS

(a) Except as provided in paragraph (b) of this section, the prior approval of the Secretary is required in respect to any loan to be made to two or more borrowers who become jointly and severally liable, or jointly liable therefor, and who will acquire an undivided interest in the property to be purchased or who will otherwise share in the proceeds of the loan, or in respect to any loan to be made to an eligible veteran whose interest in the property owned, or to be acquired with the loan proceeds, is an undivided interest only, unless such interest is at least a 50 percent interest in a partnership. The amount of the guaranty or insurance credit shall be computed in such cases only on that portion of the loan allocable to the eligible veteran which, taking into consideration all relevant factors, represents the proper contribution of the veteran to the transaction. Such loans shall be secured to the extent required by 38 U.S.C. Chapter 37 and the regulations concerning guaranty or insurance of loans to veterans.

(b) Notwithstanding the provisions of paragraph (a) of this section, the joinder of the spouse of a veteran-borrower in the ownership of residential property shall not require prior approval or preclude the issuance of a guaranty or insurance credit based upon the entire amount of the loan. If both spouses be eligible veterans, either or both may, within permissible maxima, utilize available guaranty or insurance entitlement.

(c) For the purpose of determining the rights and the liabilities of the Secretary with respect to a loan subject to paragraph (a) of this section, credits legally applicable to the entire loan shall be applied as follows:

(1) Prepayments made expressly for credit to that portion of the indebtedness allocable to the veteran (including the gratuity paid pursuant to former provisions of law), shall be applied to such portion of the indebtedness. All other payments shall be applied ratably to those portions of the loan allocable respectively to the veteran and to the other debtors.

(2) Proceeds of the sale or other liquidation of the security shall be applied ratably to the respective portions of the loan, such portion of the proceeds as represents the interest of the veteran being applied to that portion of the loan allocable to such veteran.

§36.4308 TRANSFER OF TITLE BY BORROWER OR MATURITY BY DEMAND OR ACCELERATION

(a) Except as provided by paragraphs (b) or (c) of this section the conveyance of or other transfer of title to property by operation of law or otherwise, after the creation of a lien thereon to secure a loan which is guaranteed or insured in whole or in part by the Secretary, shall not constitute an event of default, or acceleration of maturity, elective or otherwise, and shall not of itself terminate or otherwise affect the guaranty or insurance.

(b) (1) The Secretary may issue guaranty on loans in which a State, Territorial, or local governmental agency provides assistance to a veteran for the acquisition of a dwelling. Such loans will not be considered ineligible for guaranty if the State, Territorial, or local authority, by virtue of its laws or regulations or by virtue of Federal law, requires the acceleration of maturity of the loan upon the sale or conveyance of the security property to a person ineligible for assistance from such authority.

(2) At the time of application for a loan assisted by a State, Territorial, or local governmental agency, the veteran-applicant must be fully informed and consent in writing to the housing authority restrictions. A copy of the veteran's consent statement must be forwarded with the loan application or the report of a loan processed on the automatic basis.
(Authority: 38 U.S.C. 3703(c))

(c) Any housing loan which is financed under 38 U.S.C. chapter 37, and to which section 3714 of that chapter applies, shall include a provision in the security instrument that the holder may declare the loan immediately due and payable upon transfer of the property securing such loan to any transferee unless the acceptability of the assumption of the loan is established pursuant to section 3714.

(1) A holder may not exercise its option to accelerate a loan upon:

(i) The creation of a lien or other encumbrance subordinate to the lender's security instrument which does not relate to the transfer of rights of occupancy in the property;

(ii) The creation of a purchase money security interest for household appliances;

(iii) A transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

(iv) The granting of a leasehold interest of three years or less not containing an option to purchase;

(v) A transfer to a relative resulting from the death of a borrower;

(vi) A transfer where the spouse or children of the borrower become joint owners of the property with the borrower;

(vii) A transfer resulting from a decree of a dissolution of marriage, legal separation agreement, or from an incidental property settlement agreement by which the spouse of the borrower becomes the sole owner of the property. In such a case the borrower shall have the option of applying directly to the Department of Veterans Affairs regional office of jurisdiction for a release of liability in accordance with §36.4323 of this part; or

(viii) A transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property.

(2) The mortgage or deed of trust and the promissory note or bond evidencing a loan to which this paragraph applies shall bear in a conspicuous position in capital letters on the first page of the document in type at least 2 1/2 times larger than the regular type on such page the following warning: "THIS LOAN IS NOT ASSUMABLE WITHOUT THE APPROVAL OF THE DEPARTMENT OF VETERANS AFFAIRS OR ITS AUTHORIZED AGENT." Due to the difficulty in obtaining some commercial type sizes which are exactly 2 1/2 times larger in height than other sizes, minor deviations in size will be permitted based on commercially available type sizes nearest to 2 1/2 times the size of the print on the document. A similar warning in regular size type must appear on every assumption statement provided on a loan to which this paragraph applies. (Authority: 38 U.S.C. 3704 and 3714)

(d) The term of payment of any guaranteed or insured obligation shall bear a proper relation to the borrower's present and anticipated income and expenses (except loans pursuant to 38 U.S.C. 3710(a)(8) or (9)(B)(i)). In addition the terms of payment of any guaranteed or insured obligation shall provide for discharge of the obligation at a definite date or dates or intervals, in amounts specified on or computable from the face of the instrument. A loan which is payable on demand, or at sight, or on presentation, or at a time not specified or computable from the language in the note, mortgage, or other loan instrument, or which contemplates periodic renewals at the option of the holder to satisfy the repayment requirements of this section, is not eligible for guaranty or insurance, except as provided in paragraph (f) of this section.

(e) No guaranteed or insured obligation shall contain a provision to the effect that the holder shall have the right to declare the indebtedness due, or to pursue one or more legal or equitable remedies, if holder "shall feel insecure," or upon the occurrence of one or more such conditions optional to the holder, without regard to an act or omission by the debtor, which condition by the terms of the note, mortgage, or other loan instrument would at the option of the holder afford a basis for declaring a default.

(f) Notwithstanding the inclusion in the guaranteed or insured obligation of a provision contrary to the provisions of this section, the right of the holder to payment of the guaranty or insurance shall not be thereby impaired, *Provided*:

(1) Default was declared or maturity was accelerated under some other provision of the note, mortgage, or other loan instrument, or

(2) Activation or enforcement of such provision is warranted under §36.4317(a), or

(3) The prior approval of the Secretary was obtained. (Authority: 38 U.S.C. 3703(c))

(g) The holder of any guaranteed or insured obligation shall have the right, notwithstanding the absence of express provision therefor in the instruments evidencing

the indebtedness, to accelerate the maturity or such obligation at any time after the continuance of any default for the period specified in §36.4316.

(h) If sufficient funds are tendered to bring a delinquency current at any time prior to a judicial or statutory sale or other public sale under power of sale provisions contained in the loan instruments to liquidate any security for a guaranteed loan, the holder shall be obligated to accept the funds in payment of the delinquency unless:

(1) The prior approval of the Secretary is obtained to do otherwise, or

(2) Reinstatement of the loan would adversely affect the dignity of the lien or be otherwise precluded by law.

A delinquency will include all installment payments (principal, interest, taxes, insurance, advances, etc.) due and unpaid and any accumulated late charges, plus any reasonable expenses incurred and paid by the holder if termination proceedings have begun (e.g., advertising costs, foreclosure costs, attorney or trustee fees, recording fees, etc.). (Authority: 38 U.S.C. 3703(c)(1)) (Authority: 38 U.S.C. 501(a), 3703(c), 3712(g))

§36.4309 AMORTIZATION

(a) All loans, the maturity date of which is beyond 5 years from date of loan or date of assumption by the veteran, shall be amortized. Except as provided in paragraph (e) of this section, the schedule of payments thereon shall be in accordance with any generally recognized plan of amortization requiring approximately equal periodic payments and shall require a principal reduction not less often than annually during the life of the loan. The final installment on any loan shall not be in excess of two times the average of the preceding installments, except that on a construction loan such installment may be for an amount not in excess of 5 per centum of the original principal amount of the loan. The limitations imposed herein on the amount of the final installment shall not apply in the case of any loan extended pursuant to §36.4314(a).

(b) Any plan of repayment on loans required to be amortized which does not provide for a approximately equal periodic payments shall not be eligible unless the plan conforms with the provisions of paragraph (e) of this section, or is otherwise approved by the Secretary.

(c) Every guaranteed or insured loan shall be repayable within the estimated economic life of the property securing the loan.

(d) Subject to paragraph (a) of this section, any amounts which under the terms of a loan do not become due and payable on or before the last maturity date permissible for loans of its class under the limitations contained in 38 U.S.C. Chapter 37 shall automatically fall due on such date. (See §36.4334.)

(e) A graduated payment mortgage loan, providing for deferrals of interest during the first 5 years of the loan and addition of the deferred amounts to principal shall be eligible, *Provided*:

(1) The loan is for the purpose of acquiring a single-family dwelling unit, including a condominium unit or simultaneously acquiring and improving a previously occupied, existing single-family dwelling unit.

(2) (i) For proposed construction or existing homes not previously occupied (new homes), the maximum loan amount cannot exceed 97.5 percent of the lesser of the reasonable value of the property as of the time the loan is made or the purchase price.

(ii) For previously occupied, existing homes the maximum loan amount must be computed to assure that the principal amount of the loan, including all interest scheduled to be deferred and added to the loan principal, will not exceed the purchase price or reasonable value of the property, whichever is less, as of the time the loan is made;

(3) The increases in the monthly periodic payment amount occur annually on each of the first five annual anniversary dates of the first loan installment due date, at a rate of 7.5 percent over the preceding year's monthly payment amount;

(4) Beginning with the payment due on the fifth annual anniversary date of the first loan installment due date, all remaining monthly periodic payments are approximately equal in amount and amortize the loan fully in accordance with the requirements of this section, and

(5) The plan is otherwise acceptable to the Secretary. (Authority: 38 U.S.C. 3703(d)) (Authority: 38 U.S.C. 501(a), 1803(c)(1))

§36.4310 PREPAYMENT

The debtor shall have the right to prepay at any time, without premium or fee, the entire indebtedness or any part thereof not less than the amount of one installment, or $100, whichever is less. Any prepayment in full of the indebtedness shall be credited on the date received, and no interest may be charged thereafter. Any partial prepayment made on other than an installment due date need not be credited until the next following installment due date or 30 days after such prepayment, whichever is earlier. The holder and the debtor may agree at any time that any prepayment not previously applied in satisfaction of matured installments shall be reapplied for the purpose of curing or preventing any subsequent default.

§36.4311 INTEREST RATES

(a) Excepting loans guaranteed or insured pursuant to guaranty or insurance commitments issued by VA which specify an interest rate in excess of 7-1/2 per centum per annum, effective August 12, 1992, the interest rate on any home or condominium loan, other than a graduated payment mortgage loan, guaranteed or insured wholly or in part on or after such date may not exceed 7-1/2 per centum per annum on the unpaid principal balance.

(b) Excepting loans guaranteed or insured pursuant to guaranty or insurance commitments issued by VA which specify an interest rate in excess of 7-3/4 per centum per annum, effective August 12, 1992, the interest rate of any graduated payment mortgage loan guaranteed or insured wholly or in part on or after such date may not exceed 7-3/4 per centum per annum. (Authority: 38 U.S.C. 3703(c)(1))

(c) Effective August 12, 1992, the interest rate on any loan solely for energy conservation improvements or other alterations, improvements or repairs, which is guaranteed or insured wholly or in part on or after such date may not exceed 9 per centum per annum on the unpaid principal balance. (Authority: 38 U.S.C. 3703(c)(1))

(d) Interest in excess of the rate reported by the lender when requesting evidence of guaranty or insurance shall not be payable on any advance, or in the event of any delinquency or default: *Provided*, That a late charge not in excess of an amount equal to 4 percent on any installment, paid more than 15 days after due date shall not be considered a violation of this limitation.

(e) Refinancing loans for the purpose of an interest rate reduction (38 U.S.C. 3710(a)(8) or (9)(B)(i)) may specify an interest rate in excess of the rate specified in paragraph (a), (b) and (c) of this section provided the interest rate of the refinancing loan is less than the interest rate of the current VA loan being refinanced. (Authority: 38 U.S.C. 3703(c)(1) and 3710(c))

§36.4312 CHARGES AND FEES

(a) No charge shall be made against, or paid by, the borrower incident to the making of a guaranteed or insured loan other than those expressly permitted under paragraph (d) or (e) of this section, and no loan shall be guaranteed or insured unless the lender certifies to the Secretary that it has not imposed and will not impose any charges or fees against the borrower in excess of those permissible under paragraph (d) or (e) of this section. Any charge which is proper to make against the borrower under the provisions of this paragraph may be paid out of the proceeds of the loan: *Provided,* That if the purpose of the loan is to finance the purchase or construction of residential property the costs of closing the loan including the pro rata portion of the ground rents, hazard insurance premiums, current year's taxes, and other prepaid items normally involved in financing such transaction may not be included in the loan.

(b) Except as provided in the regulations concerning the guaranty or insurance of loans to veterans, no brokerage or service charge or their equivalent may be charged against the debtor or the proceeds of the loan either initially, periodically, or otherwise.

(c) Brokerage or other charges shall not be made against the veteran for obtaining any guaranty or insurance under 38 U.S.C. chapter 37, nor shall any premiums for insurance on the life of the borrower be paid out of the proceeds of a loan.

(d) The following schedule of permissible fees and charges shall be applicable to all VA guaranteed or insured loans:

(1) The veteran may pay reasonable and customary amounts for any of the following items:

(i) Fees of Department of Veterans Affairs appraiser and of compliance inspectors designated by the Department of Veterans Affairs except appraisal fees incurred for the predetermination of reasonable value requested by others than veteran or lender.

(ii) Recording fees and recording taxes or other charges incident to recordation.

(iii) Credit report.

(iv) That portion of taxes, assessments, and other similar items for the current year chargeable to the borrower and an initial deposit (lump-sum payment) for the tax and insurance account.

(v) Hazard insurance required by §36.4326.

(vi) Survey, if required by lender or veteran; except that any charge for a survey in connection with a loan under §§36.4356 through 36.4360a (condominium loans) must have the prior approval of the Secretary.

(vii) Title examination and title insurance, if any.

(viii) Such other items as may be authorized in advance by the Chief Benefits Director as appropriate for inclusion under this paragraph as proper local variances.

(2) A lender may charge and the veteran may pay a flat charge not exceeding 1 percent of the amount of the loan, provided that such flat charge shall be in lieu of all other charges relating to costs of origination not expressly specified and allowed in this schedule.

(3) In cases where a lender makes advances to a veteran during the progress of construction, alteration, improvement, or repair, either under a commitment of the Department of Veterans Affairs to issue a guaranty certificate or insurance credit upon completion, or where the lender would be entitled to guaranty or insurance on such advances when reported under automatic procedure, the lender may make a charge against the veteran of not exceeding 2 percent of the amount of the loan for its services in supervising the making of advances and the progress of construction notwithstanding that the "holdback" or final advance is not actually paid out until after the construction, alteration, improvement, or repair is fully completed: *Provided*, That the major portion (51 percent or more) of the loan proceeds is paid out during the actual progress of the construction, alteration, improvement, or repair. Such charge may be in addition to the 1 percent charge allowed under paragraph (d)(2) of this section.

(4) In construction, alteration, improvement or repair loans, including supplemental loans made pursuant to §36.4355, where no charge is permissible under the provisions of paragraph (d)(3) of this section the lender may charge and the veteran may pay a flat sum not exceeding 1 percent of the amount of the loan. Such charge may be in addition to the 1 percent allowed under paragraph (d)(2) of this section.

(5) The fees and charges permitted under this paragraph are maximums and are not intended to preclude a lender from making alternative charges against the veteran which are not specifically authorized in the schedule provided the imposition of such alternative charges would not result in an aggregate charge or payment in excess of the prescribed maximum.

(6) **Allowable Discounts**. The veteran borrower subject to the limitations set forth in paragraphs (d)(6) and (7) of this section may pay a discount required by a lender when the proceeds of the loan will be used for any of the following purposes:

(i) To refinance existing indebtedness pursuant to 38 U.S.C. 3710(a)(5), (8), or (9)(B)(i), or (ii);

(ii) To repair, alter or improve a dwelling owned by the veteran pursuant to 38 U.S.C. 3710(a)(4) or (7) if such loan is to be secured by a first lien;

(iii) To construct a dwelling or farm residence on land already owned or to be acquired by the veteran, provided that the veteran did not or will not acquire the land directly or indirectly from a builder or developer who will be constructing such dwelling or farm residence;

(iv) To purchase a dwelling from a class of sellers which the Secretary determines are legally precluded under all circumstances from paying such a discount if the best interest of the veteran would be so served.

(7) **Computation of Discounts**

(i) **Computation of Discount - Loans Secured by a First Lien**. Unless otherwise approved by the Secretary, the discount, if any, to be paid by the borrower may not exceed the difference between the bid price, rounded to the lower whole number, and par value for GNMA (Government National Mortgage Association) 90-day forward bid closing price for pass through securities 1/2 percent less than the face note rate of the loan. Unless the lender and borrower negotiate a firm written commitment for a maximum amount of discount to be paid, the bid price to be used in the computation must be the GNMA 90-day forward bid closing quote for any day 1 to 4 business days prior to loan closing. "Loan closing" is defined for this purpose as the date on which the borrower's 3-day right of rescission commences pursuant to the Truth in Lending Act. If the lender and borrower choose to negotiate a firm discount commitment for a maximum amount of discount to be paid, the bid price to be used in establishing the maximum discount must be the closing quote for the business day prior to the date of the commitment. Lenders negotiating firm commitments must close that loan at a discount no higher than the firm commitment regardless of changes in the maximum allowable Department of Veterans Affairs interest rate. If a lender's commitment expires prior to loan closing, the lender and borrower may negotiate a new firm commitment based on the procedure outlined in this paragraph (d)(7)(i) or may use the procedure for determining the discount based on the GNMA 90-day forward bid closing quote for any day 1 to 4 business days prior to loan closing.

(ii) **Computation of Discount - Unsecured Loans or Loans Secured by Less than a First Lien**. The borrower, subject to the limitations set forth in paragraph (d)(6) and (7) of this section, may pay a discount required by the lender when the proceeds of the loan will be used to repair, alter, or improve a dwelling owned by the veteran pursuant to 38 U.S.C. 3710(a)(4) or (7) if such loan is unsecured or secured by less than a first lien. No such discount may be charged unless:

(A) The loan is submitted to the Secretary for prior approval;

(B) The dollar amount of the discount is disclosed to the Secretary and the veteran prior to the issuance by the Secretary of the certificate of commitment. Said certificate of commitment shall specify the discount to be paid by the veteran, and this discount may not be increased once the commitment is issued without the approval of the Secretary;

(C) The discount has been determined by the Secretary to be reasonable in amount.

(iii) A veteran may pay the discount on an acquisition and improvement loan (as defined in §36.4301) provided:

(A) The veteran pays no discount on the acquisition portion of the loan except in accordance with paragraph (d)(6)(iv) of this section; and

(B) The discount paid on the improvements portion of the loan does not exceed the percentage of discount paid on the acquisition portion of the loan.

Acquisition and improvement loans may be closed either on the automatic or prior approval basis.

(iv) Unless the Chief Benefits Director otherwise directs, all powers of the Secretary under paragraph (d)(6) and (7) of this section are hereby delegated to the officials designated by §36.4342(b). (Authority: 38 U.S.C. 3703(c)(1) and (3), 3710(a))

(8) On any loan to which section 3714 of 38 U.S.C., chapter 37 applies, the holder may charge a reasonable fee, not to exceed the lesser of (i) $300 and the actual cost of any credit report required, or (ii) any maximum prescribed by applicable State law, for processing an application for assumption and changing its records. (Authority: 38 U.S.C. 3714)

(e) (1) Subject to the limitations set out in paragraphs (e)(4) and (e)(5) of this section, a fee must be paid to the Secretary. The fee shall be 1.25 percent of the total loan amount on all refinancing loans and for all loans for the purchase or construction of a home on which the veteran does not make a downpayment. On purchase or construction loans on which the veteran makes a downpayment of 5 percent or more, but less than 10 percent, the amount of the funding fee shall be 0.75 percent of the total loan amount. On purchase or construction loans on which the veteran makes a downpayment of 10 percent or more, the amount of the funding fee shall be 0.5 percent of the total loan amount. All or part of such fee may be paid in cash at loan closing or all or part of the fee may be included in the loan without regard to the reasonable value of the property or the computed maximum loan amount, as appropriate. In computing the fee, the lender will disregard any amount included in the loan to enable the borrower to pay such fee. (Authority: 38 U.S.C. 3729(a))

(2) Subject to the limitations set out in this section, a fee of one-half of one percent of the loan balance must be paid to the Secretary in a manner prescribed by the Secretary by a person assuming a loan to which section 3714 of title 38 U.S.C. applies. The instrument securing such a loan shall contain a provision describing the right of the holder to collect this fee as trustee for the Department of Veterans Affairs. The loan holder shall list the amount of this fee in every assumption statement provided and include a notice that the fee must be paid to the holder immediately following loan settlement. The fee must be transmitted to the Secretary within 15 days of the receipt by the holder of the notice of transfer. (Authority: 38 U.S.C. 3714, 3729(d))

(3) The lender is required to pay to the Secretary the fee described in paragraph (e)(1) of this section within 15 days after loan closing. Any lender closing a loan, subject to the limitations set out in paragraphs (e)(4) and (e)(5) of this section who fails to submit timely payment of this fee will be subject to a late charge equal to 4 percent of the total fee due. If payment of the fee described in paragraph (e)(1) of this section is made more than 30 days after loan closing, interest will be assessed at a rate set in conformity with the Department of Treasury's Fiscal Requirements Manual. This interest charge is in addition to the 4 percent late charge, but the late charge is not included in the amount on which interest is computed. This interest charge is to be calculated on a daily basis beginning on the date of closing, although the interest will be assessed only on funding fee payments received more than 30 days after closing.

(4) The fee described in paragraph (e)(1) and (e)(2) of this section shall not be collected from a veteran who is receiving compensation (or who but for the receipt of retirement pay would be entitled to receive compensation) or from a surviving spouse

described in section 3701(b) of title 38, United States Code. (Authority: 38 U.S.C. 3729(b))

§36.4313 ADVANCES AND OTHER CHARGES

(a) A holder may advance any amount reasonably necessary and proper for the maintenance or repair of the security, or for the payment of accrued taxes, special assessments, ground or water rents, or premiums on fire or other casualty insurance against loss of or damage to such property and any such advance so made may be added to the guaranteed or insured indebtedness. A holder may also advance the one-half of one percent funding fee due on a transfer under 38 U.S.C. 3714 when this is not paid at the time of transfer. All security instruments for loans to which 38 U.S.C. 3714 applies must include a clause authorizing the collection of an assumption funding fee and an advance for this fee if it is not paid at the time of transfer. (Authority: 38 U.S.C. 3714)

(b) In addition to advances allowable under paragraph (a) of this section, the holder may charge against the proceeds of the sale of the security; against gross amounts collected; in any accounting to the Secretary after payment of a claim under the guaranty in the computation of a claim under the guaranty, if lawfully authorized by the loan agreement and subject to §36.4321(a) or, in the computation of an insurance loss, any of the following items actually paid:

(1) Any expense which is reasonably necessary for preservation of the security,

(2) Court costs in a foreclosure or other prior judicial proceeding involving the security,

(3) Other expenses reasonably necessary for collecting the debt, or repossession or liquidation of the security,

(4) Reasonable trustee's fees or commissions not in excess of those allowed by statute and in no event in excess of 5 percent of the unpaid indebtedness,

(5) Reasonable amount for legal services actually performed not to exceed 10 percent of the unpaid indebtedness as of the date of the first uncured default, or $700, whichever is less,

(6) The cost of a credit report(s) on the debtor(s), which is (are) to be forwarded to the Secretary in connection with the claim,

(7) Reasonable and customary costs of property inspections,

(8) Any other expense or fee that is approved in advance by the Secretary. (Authority: 38 U.S.C. 3720(a)(3))

In no event may the combined total of the amounts claimed for trustee's fees and legal services (par. (b)(4) and (5) of this section) exceed $700. (Authority: 38 U.S.C. 3712(g), 3720(a)(3))

(c) Any advances or charges enumerated in paragraph (a) or (b) of this section may be included as specified in the holder's accounting to the Secretary, but they are not chargeable to the debtor unless he or she otherwise be liable therefor.

(d) Advances of the type enumerated in paragraph (a) of this section and any other advances determined to be necessary and proper in order to preserve or protect the security may be authorized by employees designated in §36.4342(b) in the case of any property constituting the
security for a loan acquired by the Secretary or constituting the security for the unpaid balance of the purchase price owing to the Secretary on account of the sale of such property. Such advances shall be secured to the extent legal and practicable by a lien on the property.

(e) Notwithstanding the provisions of paragraph (a) and (b) of this section, holders of condominium loans guaranteed or insured under 38 U.S.C. 3710(a)(6) shall not pay those assessments or charges allocable to the condominium unit which are provided for in the instruments establishing the condominium form of ownership in the absence of the prior approval of the Secretary.

§36.4314 EXTENSIONS AND REAMORTIZATIONS

(a) Provided the debtor(s) is (are) a reasonable credit risk(s), as determined by the holder based upon review of the debtor's(s') creditworthiness, including a review of a current credit report(s) on the debtor(s), the terms of repayment of any loan may by written agreement between the holder and the debtor(s), be extended in the event of default, to avoid imminent default, or in any other case where the prior approval of the Secretary is obtained. Except with the prior approval of the Secretary, no such extension shall set a rate of amortization less than that sufficient to fully amortize at least 80 percent of the loan balance so extended within the maximum maturity prescribed for loans of its class.

(b) In the event of a partial prepayment pursuant to §36.4310 the balance of the indebtedness may, by written agreement between the holder the debtor(s), be reamortized, provided the reamortization schedule will result in full repayment of the loan within the original maturity, and provided the debtor(s) is (are) reasonable credit risk(s), as determined by the holder based upon review of the debtor's(s') creditworthiness, including a review of a current credit report(s) on the debtor(s).

(c) In the event an additional loan is proposed to be made pursuant to §36.4351 for the repair, alteration, or improvement of real property on which there is an existing loan guaranteed or insured under 38 U.S.C. chapter 37, the terms of repayment of the prior loan may, by written agreement between the holder and the debtor, be recast to combine the schedule of repayments on the two loans, provided the entire indebtedness is repayable within the permissible maximum maturity of the original loan.

(d) Unless the prior approval of the Secretary has been obtained, any extension or reamortization agreed to by a holder which relieves any obligor from liability will release the liability of the Secretary under the guaranty or insurance on the entire loan. However, if such release of liability of an obligor results through operation of law by reason of an extension or other act of forbearance, the liability of the Secretary as guarantor or insurer will not be affected thereby, provided the required lien is maintained and the title holder is and will remain liable for the payment of the indebtedness: *And further provided*, That if such extension or act of forbearance will result in the release of the veteran, all delinquent installments, plus any foreclosure expenses which may have been incurred, shall have been fully paid.

(e) The holder shall promptly forward to the Secretary an advice of the terms of any agreement effecting a reamortization or extension of a guaranteed or insured loan,

together with a cop(y)(ies) of the credit report(s) obtained on the debtor(s). (Authority: 38 U.S.C. 3703(c)(1))

§36.4315 NOTICE OF DEFAULT AND ACCEPTABILITY OF PARTIAL PAYMENTS

(a) **Reporting of Defaults**. The holder of any guaranteed or insured loan shall give notice to the Secretary within 45 days after any debtor:

(1) Is in default by reason of nonpayment of any installment for a period of 60 days from the date of first uncured default (see §36.4301(f)); or

(2) Is in default by failing to comply with any other covenant or obligation of such guaranteed or insured loan which failure persists for a continuing period of 90 days after demand for compliance therewith has been made, except that if the default is due to nonpayment of real estate taxes, the notice shall not be required until the failure to pay when due has persisted for a continuing period of 180 days.

(b) Partial Payments. A partial payment is a remittance on a loan in default (as defined in §36.4301(g)) of any amount less than the full amount due under the terms of the loan and security instruments at the time the remittance is tendered.

(1) Except as provided in paragraph (b)(2) of this section, or upon the express waiver of the Secretary, the mortgage holder shall accept any partial payment and either apply it to the mortgagor's account or identify it with the mortgagor's account and hold it in a special account pending disposition. When partial payments held for disposition aggregate a full monthly installment, including escrow, they shall be applied to the mortgagor's account.

(2) A partial payment may be returned to the mortgagor, within 10 calendar days from date of receipt of such payment, with a letter of explanation only if one or more of the following conditions exist:

(i) The property is wholly or partially tenant-occupied and rental payments are not being remitted to the holder for application to the loan account;

(ii) The payment is less than one full monthly installment, including escrows and late charge, if applicable, unless the lesser payment amount has been agreed to under a written repayment plan;

(iii) The payment is less than 50 percent of the total amount then due unless the lesser payment amount has been agreed to under a written repayment plan;

(iv) The payment is less than the amount agreed to in a written repayment plan;

(v) The amount tendered is in the form of a personal check and the holder has previously notified the mortgagor in writing that only cash or certified remittances are acceptable;

(vi) A delinquency of any amount has continued for at least 6 months since the account first became delinquent and no written repayment plan has been arranged;

(vii) Foreclosure has been commenced by the taking of the first action required for foreclosure under local law;

(viii) The holder's lien position would be jeopardized by acceptance of the partial payment.

(3) A failure by the holder to comply with the provisions of this paragraph may result in a partial or total loss of guaranty or insurance pursuant to §36.4325(b), but such failure shall not constitute a defense to any legal action to terminate the loan. (Authority: 38 U.S.C. 3703(c)(1))

§36.4316 CONTINUED DEFAULT

(a) In the event any failure of the debtor to discharge the debtor's obligations under the loan continues for a period of 3 months, or for more than 1 month on an extended loan or on a term loan, the holder may at the holder's option then or thereafter, submit a claim for payment of the guaranty. The holder may also then or thereafter give the notice prescribed in §36.4317.

(b) A claim for the guaranty, or the notice prescribed in §36.4317 may be submitted prior to the time prescribed in paragraph (a) of this section in any case where any material prejudice to the rights of the holder or to the Secretary or hazard to the security warrants more prompt action.

(c) A claim for the guaranty must include a copy(ies) or a current credit report(s) on the debtor(s). (Authority: 38 U.S.C. 3732)

§36.4317 NOTICE OF INTENTION TO FORECLOSE

(See also §36.4319.) Except upon the express waiver of the Secretary, a holder shall not begin proceedings in court or give notice of sale under power of sale, other otherwise take steps to terminate the debtor's rights in the security until the expiration of 30 days after delivery by registered mail to the Secretary of a notice of intention to take such action: *Provided*, That:

(a) Immediate action as required under 38 CFR 36.4346(i), may be taken if the property to be affected thereby has been abandoned by the debtor, or has been or may be otherwise subjected to extraordinary waste or hazard, or if there exist conditions justifying the appointment of a receiver for the property (without reference to any contractual provisions for such appointment);

(b) Any right of a holder to repossess personal property may be exercised without prior notice to the Secretary; but notice of any such action taken shall be given by certified mail to the Secretary within ten days thereafter; and

(c) The notice required under this paragraph shall also be provided to the original veteran-borrower and any other liable obligors by certified mail within 30 days after such notice is provided to the Secretary in all cases in which the current owner of the property is not the original veteran-borrower. A failure by the holder to make a good faith effort to comply with the provisions of this subparagraph may result in a partial or total loss of guaranty or insurance pursuant to VA Regulation 36.4325(b), but such faillure shall not constitute a defense to any legal action to terminate the loan. A good faith effort will include, but is not limited to:

(1) A search of the holder's automated and physical loan record systems to identify the name and current or last known address of the original veteran and any other liable obligors;

(2) A search of the holder's automated and physical loan record systems to identify sufficient information (e.g., Social Security Number) to perform a routine trace inquiry through a major consumer credit bureau;

(3) Conducting the trace inquiry using an in-house credit reporting terminal;

(4) Obtaining the results of the inquiry;

(5) Mailing the required notices and concurrently providing the Secretary with the names and addresses of all obligors identified and sent notice; and,

(6) Documentation of the holder's records.

§36.4318 REFUNDING OF LOANS IN DEFAULT

(a) Upon receiving a notice of default or a claim for a guaranty or a notice under §36.4317, the Secretary may within 30 days thereafter require the holder upon penalty of otherwise losing the guaranty or insurance to transfer and assign the loan and the security therefor to the Secretary or to another designated by the Secretary upon receipt of payment in full of the balance of the indebtedness remaining unpaid to the date of such assignment. Such assignment may be made without recourse but the transferor shall not thereby be relieved from the provisions of §36.4325.

(b) If the obligation is assigned or transferred to a third party pursuant to paragraph (a) of this section, the Secretary may continue in effect the guaranty or insurance issued with respect to the previous loan in such manner as to cover the assignee or transferee.

§36.4319 LEGAL PROCEEDINGS

(a) When the holder institutes suit or otherwise becomes a party in any legal or equitable proceeding brought on or in connection with the guaranteed or insured indebtedness, or involving title to, or other lien on, the security, such holder, within the time that would be required if the Secretary were a party to the proceeding, shall deliver to the Secretary, by mail or otherwise, by making such delivery to the Loan Guaranty Officer at the office which granted the guaranty or the insurance, or other office to which the holder has been notified the file is transferred, a copy of every procedural paper filed on behalf of holder, and shall also so deliver, as promptly as possible, a copy of each similar pleading served on holder or filed in the cause by any other party thereto. Notice of, or motion for, continuance and orders thereon are excepted from the foregoing.

(b) A copy of a notice of sale shall be similarly delivered by the holder, or the holder's agent or trustee, to the Secretary at the VA Regional Office of jurisdiction at least 30 days prior to the scheduled liquidation sale, or within 5 days after the date of first publication of the notice, whichever is later. A copy of any other notice of sale or acquisition of the property served on the holder or advice of any sale of which the holder has knowledge shall be similarly delivered to the Secretary, including any such notice of a tax sale or other superior lien or judicial sale. Such notice shall be accompanied by a statement of the account indebtedness and a copy of the liquidation appraisal request, if not previously delivered. (Authority: 38 U.S.C. 3732)

(c) The procedure prescribed in paragraph (a) and (b) of this section shall not be applicable in any proceeding to which the Secretary is a party, after the Secretary's appearance shall have been entered therein by a duly authorized attorney.

(d) In any legal or equitable proceeding (including probate and bankruptcy proceedings) to which the Secretary is a party, original process and any other process prior to appearance, proper to be served on the Secretary, shall be delivered to the Loan Guaranty Officer of the regional office of the VA having jurisdiction of the area in which the court is situated. Within the time required by applicable law, or rule of court, the Secretary will cause appropriate special or general appearance to be entered in the case by an authorized attorney. (Authority: 38 U.S.C. 3732)

(e) After appearance of the Secretary by attorney all process and notice otherwise proper to serve on the Secretary before or after judgment, if served on the attorney of record, shall have the same effect as if the Secretary were personally served within the jurisdiction of the court. (Authority: 38 U.S.C. 3732)

(f) If following a default, the holder does not bring appropriate action within 30 days after requested in writing by the Secretary to do so, or does not prosecute such action with reasonable diligence, the Secretary may at the Secretary's option fix a date beyond which no further charges may be included in the computation of the indebtedness for the purposes of accounting between the holder and the Secretary. The Secretary may also intervene in, or begin and prosecute to completion any action or proceeding in the Secretary's name or in the name of the holder, which the Secretary deems necessary or appropriate. The Secretary shall pay, in advance if necessary, any court costs or other expenses incurred by the Secretary or properly taxed against the Secretary in any such action to which the Secretary is a party, but may charge the same, and also a reasonable amount for legal services, against the guaranteed or insured indebtedness, or the proceeds of the sale of the security to the same extent as the holder (see §36.4313 of this part), or otherwise collect from the holder any such expenses incurred by the Secretary because of the neglect or failure of the holder to take or complete proper action. The rights and remedies herein reserved are without prejudice to any other rights, remedies, or defenses, in law or in equity, available to the Secretary. (Authority: 38 U.S.C. 3732)

§36.4320 SALE OF SECURITY

(a) Upon receipt by the Secretary of notice of a liquidation sale of any security for a guaranteed or insured loan, the Secretary shall determine the net value of the security and shall notify the holder of the net value and of the regulatory provision which will govern the disposition of the security.

(1) If the net value of the real property securing a guaranteed or insured loan exceeds the unguaranteed portion of the indebtedness, the Secretary shall specify in advance of the liquidation sale the minimum amount which shall be credited to the indebtedness of the borrower on account of the value of the security to be sold, subject to the following:

(i) The specified amount in such cases shall be the lesser of the net value of the property or the total indebtedness,

(ii) If a minimum amount for credit to the indebtedness has been specified in relation to a liquidation sale of real property, and:

(A) The holder acquires the property, or the rights to the property, at the sale for an amount not in excess of such specified amount, the holder shall credit to the indebtedness the amount specified. The holder then may retain the property or, not later than 15 days after the date of sale, advise the Secretary of the holder's election to convey or transfer the property, or the rights to the property, to the Secretary;

(B) The holder acquires the property, or the rights to the property, at the liquidation sale for an amount in excess of the specified amount, the indebtedness shall be credited with the proceeds of the sale. The holder shall not have the option to convey the property to the Secretary unless a bid in excess of the specified amount was made pursuant to paragraph (a)(3) of this section;

(C) A third party acquires the property, or the rights to the property, at the liquidation sale for an amount equal to or in excess of that specified, the holder shall credit to the indebtedness the net proceeds of the sale;

(D) A third party acquires the property, or the rights to the property, at the liquidation sale for an amount less than that specified, the holder shall credit to the indebtedness the amount specified.

(iii) If a minimum amount has been specified by the Secretary, the Secretary's liability under loan guaranty shall be the total indebtedness less the amount credited to the indebtedness under paragraph (a)(1)(ii) of this section, not to exceed the Secretary's maximum liability as computed under §36.4321 of this part.

(2) If the net value of the real property securing a guaranteed or insured loan does not exceed the unguaranteed portion of the indebtedness:

(i) The Secretary shall notify the holder that no minimum amount will be specified for credit to the indebtedness on account of the value of the security to be sold;

(ii) The Secretary may not accept conveyance or transfer of the property;

(iii) The holder shall credit against the indebtedness the net proceeds of the sale, and the Secretary's liability under loan guaranty shall be limited to the total indebtedness less the amount credited to the indebtedness not to exceed the Secretary's maximum liability as computed under §36.432l of this part; and

(iv) The liability of the Secretary shall not be subject to adjustment by reason of any subsequent disposition of the property by the holder.

(3) If a minimum bid is required under applicable State law, or decree of foreclosure or order of sale, or other lawful order or decree, and:

(i) Such minimum bid exceeds an amount which has been specified by the Secretary under paragraph (a)(1) of this section; and

(ii) The holder acquires the property at the liquidation sale for an amount not exceeding the amount legally required; the holder may elect to convey the property to the Secretary pursuant to paragraph (a)(1)(ii)(A) of this section. The amount bid at the sale or the total indebtedness, whichever is less, shall govern instead of the specified amount and for the purpose of determining the Secretary's liability under loan guaranty. (Authority: 38 U.S.C. 3732)

(b) The holder should not carry out a liquidation sale until the Secretary has furnished the notice required under paragraph (a) of this section. In the event the holder carries out a liquidation sale prior to receiving such notice, the holder shall credit against the indebtedness the greater of:

(1) The net proceeds of the sale; or

(2) The amount of the indebtedness or the net value of the property, whichever is less.

The provisions of paragraph (a)(1)(ii)(A) of this section, which extends to the holder the option of conveying or transferring the property to the Secretary, shall not be applicable, and the Secretary's liability under the loan guaranty shall be the total indebtedness less the amount credited to the indebtedness under paragraph (b)(1) or (2) of this section, not to exceed the Secretary's maximum liability as computed under §36.4321 of this part. (Authority: 38 U.S.C. 3732)

(c) When a debtor proposes to convey or transfer any real property to a holder to avoid foreclosure or other judicial, contractual, or statutory disposition of the obligation or of the security, the consent of the Secretary to the terms of such proposal shall be obtained in advance of such conveyance or transfer. In consenting to the terms of the debtor's proposal the Secretary shall furnish the notice required under paragraph (a) of this section. (Authority: 38 U.S.C. 3732)

(d) Upon receipt by the Secretary of notice of a judicial or statutory sale, or other public sale under power of sale contained in the loan instruments, to liquidate any personal property which is security for a guaranteed or insured loan, the Secretary may specify in advance of such sale the minimum amount which shall be credited to the indebtedness of the borrower on account of the value of the security to be sold.

(1) If a minimum amount has been specified by the Secretary, and

(i) The holder is the successful bidder at the sale for an amount not in excess of such minimum amount, the holder shall sell the property pursuant to paragraph (d)(3) of this section and the amount realized from the resale of the property shall govern, instead of the specified minimum amount, in the final accounting for determining the rights and liabilities of the holder and the Secretary,

(ii) A third party is the successful bidder at the sale for an amount equal to or in excess of that specified, the holder shall credit to the indebtedness the net proceeds of the sale,

(iii) A third party is the successful bidder at the sale for an amount less than that specified, the holder shall credit to the indebtedness the amount specified,

(iv) The holder is the successful bidder at the sale for an amount in excess of the specified amount, the indebtedness shall be credited with the proceeds of the sale or the amount realized from the resale of the property pursuant to paragraph (d)(3) of this section, whichever is the greater, unless the bid in excess of the specified amount was made pursuant to paragraph (d)(4) of this section.

(2) If a minimum amount has not been specified by the Secretary under paragraph (d)(1) of this section, the holder shall credit against the indebtedness the net proceeds of the sale except as provided in paragraph (d)(4) of this section.

(3) If personal property has been repossessed or otherwise acquired by a holder and no public sale is proposed or required to be held to entitle the holder to effect a further disposition of such property, or if the holder is the successful bidder at the sale of personal property as provided in paragraph (d)(1) of this section, the holder shall sell the property within a reasonable time. The holder shall submit to the Secretary a written advice setting forth the price, terms, conditions and the expenses of the proposed sale at least 10 days in advance, and the Secretary shall either assent to such sale in which event the holder shall credit against the indebtedness the net proceeds of the sale or, upon agreement to indemnify the holder to the extent of any increased or resultant loss, the Secretary may specify the minimum net price for which the security may be sold. If such amount has been specified, the holder shall sell the personal property within a reasonable time in the open market for the best price obtainable: *Provided*, that the prior approval of the Secretary shall be obtained if the property is to be sold for a net amount less than the specified amount, or if the property is to be sold on terms other than all cash. The ultimate net amount realized by the holder from such sale shall be reported by the holder to the Secretary in an accounting which will determine their respective rights and liabilities.

(4) If a minimum bid is required under applicable State law, or decree of foreclosure or order of sale, or other lawful order or decree, the holder may bid an amount not exceeding such amount legally required. If an amount has been specified by the Secretary and the holder is the successful bidder for an amount not exceeding the amount legally required, such specified amount shall govern for the purposes of this paragraph and for the purpose of computing the ultimate loss under the guaranty or insurance. In the event no amount is specified and the holder is the successful bidder for an amount not exceeding the amount legally required, the amount paid or payable by the Secretary under the guaranty shall not be subject to any adjustment by reason of such bid. (Authority: 38 U.S.C. 3732)

(e) If the Secretary has specified an amount as provided in this section, and the holder learns of any material damage to the property occurring prior to the foreclosure sale or to the acceptance of a deed in lieu of foreclosure or prior to any other event to which such specified amount is applicable, the holder shall promptly advise the Secretary of such damage.

(f) The holder in accounting to the Secretary in connection with the disposition of any property in accordance with paragraph (a), (b), or (d) of this section, may include as a part of the indebtedness all actual expenses or costs of the proceedings, paid by the holder, within the limits defined in §36.4313 of this part. In connection with the conveyance or transfer of property to the Secretary the holder may include in accounting to the Secretary the following expense items if actually paid by the holder, in addition to the consideration payable for the property under paragraph (g) of this section. (Authority: 38 U.S.C. 3732)

(1) State and documentary stamp taxes as may be required.

(2) The customary cost of obtaining evidence of title in favor of the Secretary as specified in paragraph (h)(5) of this section but not including title evidence obtained incident to the making of the loan or any expenses incurred to clear title defects.

(3) Amount expended for taxes, special assessments, including such payments which are specified in paragraph (h)(4) of this section.

(4) Recording fees.

(5) Any other expenditures in connection with the property which are approved by the Secretary.

(g) In the event a holder elects to convey or transfer the property to the Secretary pursuant to paragraph (a), (b), or (c) of this section, the consideration to be paid by the Secretary in return for the property shall be the specified amount: *Provided*, that if a claim under the guaranty was previously paid, the consideration payable for the property shall be an amount equal to the indebtedness (less the amount previously paid on the guaranty) or the specified amount, whichever is less. If no claim under the guaranty was previously paid, the holder may, pursuant to §36.4321(b) submit a claim within the maximum guaranty liability for the difference between the specified amount and an amount equal to the indebtedness. In the case of an insured loan, the holder may submit a claim for the difference between an amount equal to the indebtedness and the specified amount pursuant to §36.4374.

(h) The conveyance or transfer of any property to the Secretary pursuant to paragraphs (a), (b), or (c) of this section shall be subject to the following provisions:

(1) If the holder's notice to the Secretary electing to convey or transfer the property precedes the acquisition of the property by the holder and the holder then acquires the property, the holder shall promptly after such acquisition advise the Secretary of the acquisition. Such advice, or the notice of election if given subsequent to acquisition, shall state the amount of the successful bid (if the property was acquired by the holder at public sale) and shall state the insurance coverage then in force, specifying for each policy, the name of the insurance company, the hazard covered, the amount, and the expiration date.

(2) The holder shall not cancel any insurance in force when the holder acquires the property. Coincident with the notice of election to convey or transfer the property to the Secretary or with the acquisition of the property by the holder, following such notice, whichever is later, the holder shall obtain endorsements on all such insurance policies naming the Secretary as an assured, as his/her interest may appear. Such insurance policies shall be forwarded to the Secretary at the time of the conveyance or transfer of the property to the Secretary or as soon after that time as feasible.

(3) Occupancy of the property by anyone properly in possession by virtue of and during a period of redemption, or by any one else unless under a claim of title which makes the title sought to be conveyed by the holder of less dignity or quality than that required by this section, shall not preclude the holder from conveying or transferring the property to the Secretary. Except with the prior approval of the Secretary, the holder shall not rent the property to a new tenant, nor extend the term of an existing tenancy on other than a month-to-month basis.

(4) Any taxes, special assessments or ground rents due and payable within 30 days after date of conveyance or transfer to the Secretary shall be paid by the holder if bills therefor are obtainable before such conveyance or transfer.

(5) Each conveyance or transfer of real property to the Secretary pursuant to this section shall be acceptable if the holder thereby covenants or warrants against the acts of the holder and those claiming under the holder (e.g., by special warranty deed) and if it vests in the Secretary or will entitle the Secretary to such title as is or would be acceptable to prudent lending institutions, informed buyers, title companies, and

attorneys, generally in the community in which the property is situated. Any title so acceptable will not be unacceptable to the Secretary by reason of any of the limitations on the quantum or quality of the property or title stated in §36.4350(b) of this part:

Provided, That

(i) At the time of conveyance or transfer to the Secretary there has been no breach of any conditions affording a right to the exercise of any reverter, except that title will not be unacceptable to the Secretary by reason of a violation of a restriction based on race, color, creed, or national origin, whether or not such restriction provides for reversion or forfeiture of title or a lien for liquidated damages in the event of a breach.

(ii) With respect to any such limitations which came into existence subsequent to the making of the loan, full compliance was had with the requirements of §36.4324 of this part. The acceptability of a conveyance or transfer pursuant to the requirements of this paragraph will be established by delivery to the Secretary of any of the following evidence of title issued by an institution or person satisfactory to the Secretary, in form satisfactory to him/her showing that title to the property of the quality specified in this paragraph is or will be vested in the Secretary:

(A) A title policy insuring the Secretary in an amount approximately equal to the consideration for the property, or a commitment for such title policy; or

(B) A certificate of record title; or

(C) An abstract of title accompanied by a legal opinion as to the quality of such title of record; or

(D) A Torrens or similar title certificate; or

(E) Such other evidence of title as the Secretary may approve.

In lieu of such title evidence, the Secretary will accept a conveyance or transfer with general warranty with respect to the title from a holder described in 38 U.S.C. 3702(d) or from a holder of financial responsibility satisfactory to the Secretary. In any case where the holder does not deliver evidence of title of the character specified in this paragraph, the holder to aid the Secretary in determination of acceptability of title shall without expense to the Secretary furnish such evidence of title, including survey, if any, as may have been obtained by the holder incident to the making of the loan or attendant to the foreclosure.

(6) Except with respect to matters covered by any covenants or warranties of the holder, the acceptance by the Secretary of a conveyance or transfer by the holder shall conclude the responsibility of the holder to the Secretary under the regulations of this subpart with respect to the title and in the event of the subsequent discovery of title defects, the Secretary shall have no recourse against the holder with respect to such title other than by reason of such covenants or warranties.

(7) As between the holder and the Secretary, the responsibility for any loss due to damage to or destruction of the property or due to personal injury sustained in respect to such property shall be governed by the provisions of this paragraph and paragraph (h)(10) of this section. Ordinary wear and tear excepted, the holder shall bear such risk of loss from the date of acquisition by the holder to the date such risk of loss is assumed by the Secretary. Such risk of loss is assumed by the Secretary from the date of receipt to

the holder's election to convey or transfer the property to the Secretary or, in the event of receipt of notice of such election prior to acquisition, from the date of the Secretary's receipt of notice of acquisition by the holder:

Provided that if custody over the property has not been delivered by the holder to the Secretary on the date when the Secretary otherwise would have assumed the risk of loss, the Secretary's assumption of the risk of loss will be deferred until such custody over the property is delivered, or until the property has been conveyed or transferred to the Secretary. The amount of any loss chargeable to the holder may be deducted from the amount payable by the Secretary at the time the property is transferred. In any case where pursuant to the VA regulations rejection of the title is legally proper, the Secretary may surrender custody of the property as of the date specified in the Secretary's notice to the holder. The Secretary's assumption of such risk shall terminate upon such surrender.

(8) The holder shall not be liable to the Secretary for any portion of the paid or unpaid taxes, special assessments, ground rents, insurance premiums, or other similar items.

(9) The Secretary shall be entitled to all rentals and other income collected from the property and to any insurance proceeds or refunds subsequent to the date of acquisition by the holder.

(10) In respect to a property which was the security for a condominium loan guaranteed or insured under 38 U.S.C. 3710(a)(6) the responsibility for any loss due to damage to or destruction of the property or due to personal injury sustained in respect to such property shall in no event pass to the Secretary until the Secretary expressly assumes such responsibility or until conveyance of the property to the Secretary, whichever first occurs. The holder shall have the right to convey such property to the Secretary only if the property (including elements of the development or project owned in common with other unit owners) is undamaged by fire, earthquake, windstorm, flooding or boiler explosion. The absence of a right in the holder to convey such property which is so damaged shall not preclude a conveyance, if the Secretary agrees in a given case to such a conveyance upon completion of repairs within a specified period of time and such repairs are so completed and the conveyance is otherwise in order.

(i) (1) The terms *date of sale* or *date of acquisition* as used in this section are defined as the date of the event (e.g., sale, confirmation of sale when required under local practice, delivery of deed in case of voluntary conveyance, etc.) which fixes the rights of the parties in the property.

(2) The term *property* or *real property* as used in this section shall include:

(i) A leasehold estate which at the time of closing the loan was not less duration than prescribed by 36.4350(a)(2) of this part, and

(ii) The rights derived by the holder through a foreclosure sale of real estate whether or not such rights constitute an estate in real property under local law.

(j) Except as provided in paragraph (h)(6) of this section, the provisions of this section shall not be in derogation of any rights which the Secretary may have under §36.4325 of this part. The Chief Benefits Director, or the Director, Loan Guaranty Service, may authorize any deviation from the provisions of this section, within the limitations prescribed in 38 U.S.C. Chapter 37, which may be necessary or desirable to accomplish the objectives of this section if such deviation is made necessary by reason of

any laws or practice in any State or Territory or the District of Columbia: *Provided, that* no such deviation shall impair the rights of any holder not consenting to the deviation with respect to loans made or approved prior to the date the holder is notified of such action.

§36.4321 COMPUTATION OF GUARANTY CLAIMS; SUBSEQUENT ACCOUNTING

(a) Subject to the limitation that the total amounts payable shall in no event exceed the amount originally guaranteed, the amount payable on a claim for the guaranty shall be the percentage of the loan originally guaranteed applied to the indebtedness computed as of the earliest of the following dates:

(1) The date of the liquidation sale; or,

(2) The cutoff date established under paragraph (f) of §36.4319 of this part; or,

(3) The cutoff date established under paragraph (b) of this section.

Deposits or other credits or setoffs legally applicable to the indebtedness on the date of computation shall be applied in reduction of the indebtedness on which the claim is based. Any escrowed or earmarked funds not subject to superior claims of third persons must likewise be so applied.

(b) In any case in which there is a delay in the liquidation sale caused by:

(1) The holder of the loan extending forbearance in excess of 30 days at the request of the Secretary, the cutoff date for computation of the indebtedness shall be 30 days after the date the Secretary determines the liquidation sale would have taken place if there had been no such delay, provided: the net value of the real property securing the loan does not exceed the unguaranteed portion of the indebtedness as of the actual liquidation sale date *and* such net value will exceed the unguaranteed portion of the indebtedness as of the cutoff date;

(2) The Secretary, including the Secretary's failure to provide the holder with advice as to the net value of the security within two working days prior to a scheduled liquidation sale but excluding forbearance exercised at the request of the Secretary, with respect to a holder which has complied with the provisions of §36.4319(b) of this part, the cutoff date for computation of the indebtedness shall be the date the liquidation sale would have taken place if there had been no such delay;

(3) A voluntary case commenced under Title 11, United States Code (relating to bankruptcy), the cutoff date for computation of the indebtedness shall be 30 days after the date the Secretary determines the liquidation sale would have taken place if there had been no such delay, provided: the net value of the real property securing the loan does not exceed the unguaranteed portion of the indebtedness as of the actual liquidation sale date *and* such net value will exceed the unguaranteed portion of the indebtedness as of the cutoff date.

(c) Adjustment of cutoff dates:

(1) Any cutoff date established under §36.4319(f) of this part or paragraph (b) of this section will be adjusted by a period of months corresponding to the number of

installment payments, if any, received by the holder and credited to the indebtedness after the cutoff date is established.

(2) When a cutoff date is established under paragraph (b)(2) of this section, the actual liquidation sale date will be used for purposes of computing the indebtedness in any subsequent accounting between the holder and the Secretary; if an earlier cutoff date is in effect at the time delay in liquidation sale is caused by the Secretary, such date will not be modified by application of the provisions of paragraph (b)(2) of this section, but will be extended by an interval corresponding to the delay in the liquidation sale caused by the Secretary for purposes of computing the indebtedness in any subsequent accounting between the holder and the Secretary.

(3) Any cutoff date established under §36.4319 of this part or paragraph (b) of this section will be considered to be the liquidation sale date. Such date will be modified in accordance with paragraph (b) of this section of the provisions of that paragraph are applicable after such date has been established. (Authority: 38 U.S.C. 501(a))

(d) Credits accruing from the proceeds of a sale or other disposition of the security subsequent to the date of computation, and prior to the submission of this claim, shall be reported to the Secretary incident to such submission, and the amount payable on the claim shall in no event exceed the remaining balance of the indebtedness. (Authority: 38 U.S.C. 501(a))

(e) The claimant shall be deemed to have received as trustee for the benefit of the United States any amounts received on account of the indebtedness after the date of the claim, from the proceeds of a sale of the security or otherwise, to the extent such credits exceed the balance of the indebtedness unsatisfied by the payment of the guaranty. The claimant shall immediately pay such amounts to the Secretary to the extent of the debtor's liability to the Secretary as guarantor. (Authority: 38 U.S.C. 501(a))

§36.4322 COMPUTATION OF INDEBTEDNESS

In computing the indebtedness for the purpose of filing a claim for payment of a guaranty, or for payment of an insured loss, or in the event of a transfer of the loan under §36.4318(a), or other accounting to the Secretary, the holder shall not be entitled to treat repayments theretofore made as liquidated damages, or rentals, or otherwise than as payments on the indebtedness, notwithstanding any provision in the note, or mortgage, or otherwise, to the contrary.

§36.4323 SUBROGATION AND INDEMNITY

(a) The Secretary shall be subrogated to the contract and the lien or other rights of the holder to the extent of any sum paid on a guaranty or on account of an insured loss, which right shall be junior to the holder's rights as against the debtor or the encumbered property until the holder shall have received the full amount payable under the contract with the debtor. No partial or complete release by a creditor shall impair the rights of the Secretary with respect to the debtor's obligation.

(b) The holder, upon request, shall execute, acknowledge and deliver an appropriate instrument tendered for that purpose, evidencing any payment received from the Secretary and the Secretary's resulting right of subrogation.

(c) The Secretary shall cause the instrument required by paragraph (b) of this section to be filed for record in the office of the recorder of deeds, or other appropriate office of

the proper county, town or State, in accordance with the applicable State law. The filing or failure to file such instrument for record shall have the legal results prescribed by the applicable law of the State where the real or personal property is situated, with respect to filing or failure to so file mortgages and other lien instruments and assignments thereof.

The references herein to "filing for record" include "registration" or any similar transaction, by whatever name designated when title to the encumbered property has been "registered" pursuant to a Torrens or other similar title registration system provided by law.

(d) As a condition to paying a claim for an insured loss the Secretary may require that the loan, including any security or judgment held therefor, be assigned to the extent of such payment, and if any claim has been filed in bankruptcy, insolvency, probate, or similar proceedings such claim may likewise be required to be so assigned.

(e) Any amounts paid by the Secretary on account of the liabilities of any veteran guaranteed or insured under the provisions of 38 U.S.C., chapter 37 shall constitute a debt owing to the United States by such veteran. (Authority: 38 U.S.C. 3732)

(1) Prior to a liquidation sale, an official authorized to act for the Secretary under provisions of §36.4342 of this part may approve a complete release of the Secretary's right to collect a debt owing to the United States under this paragraph and/or under paragraph (a) of this section provided such official determines:

(i) The loan default was caused by circumstances beyond the control of the obligor;

(ii) There are no indications of fraud, misrepresentation or bad faith on the part of the obligor in obtaining the loan or in connection with the loan default;

(iii) The obligor cooperated with VA in exploring all realistic alternatives to termination of the loan through foreclosure; and, either

(iv) Review of the obligor's current financial situation and prospective earning potential and obligations indicates there are no realistic prospects that the obligor could repay all or part of the anticipated debt within six years of the liquidation sale while providing the necessities of life for himself or herself and his or her family; or,

(v) In consideration for a release of the Secretary's collection rights the obligor completes, or VA is enabled to authorize, an action which reduces the Government's claim liability sufficiently to offset the amount of the anticipated indebtedness which would otherwise be established pursuant to this paragraph and likely be collectable by VA after foreclosure in view of the obligor's financial situation; such actions would include termination of the loan by means of a deed in lieu of foreclosure, private sale of the property for less than the indebtedness with a reduced claim paid by VA for the balance due the loan holder or enabling VA to authorize the holder to elect a more expeditious foreclosure procedure when such an election would result in the legal release of the obligor's liability.

(2) Prior to a liquidation sale, an official authorized to act for the Secretary under provisions of §36.4342 of this part may approve a partial release of the Secretary's right to collect a debt owing to the United States under this paragraph and/or under paragraph (a) of this section provided such official determines:

(i) The loan default was caused by circumstances beyond the control of the obligor:

(ii) There are no indications of fraud, misrepresentation or bad faith on the part of the obligor in obtaining the loan or in connection with the loan default;

(iii) The obligor cooperated with VA in exploring all realistic alternatives to termination of the loan through foreclosure;

(iv) Review of the obligor's current financial situation and prospective earning potential and obligations indicates there are no realistic prospects that the obligor could repay all of the anticipated debt within six years of the liquidation sale while providing the necessities of life for himself or herself and his or her family; and,

(v) The obligor executes a written agreement acknowledging his or her liability to VA under this paragraph and executes a promissory note which provides for regular amortized monthly payments of an amount determined by VA in accordance with paragraph (e)(3) of this section including interest on the total amount payable at the rate in effect for Loan Guaranty liability accounts at the time of execution, or, the obligor agrees to other terms of repayment acceptable to VA including payment of a lump sum in settlement of his or her obligation under this paragraph;

(3) For purposes of this paragraph a review of an obligor's financial situation will take into consideration:

(i) The obligor's current and anticipated family income based on employment skills and experience;

(ii) The obligor's current short-term and long-term financial obligations, including the obligation to repay the Government which must be afforded consideration at least equal to his or her consumer debt obligations;

(iii) A current credit report on the obligor;

(iv) The obligor's assets and net worth; and,

(v) The required balance available for family support used in underwriting VA guaranteed loans in the area.

The amount of indebtedness established will be such that the obligor's financial situation permits repayment of the debt to the Government in regular monthly installments of principal plus interest over a five year period commencing within one year after the date the promissory note is executed, except in those cases in which a lump sum settlement appears to be in the best interest of the Government or in which it appears the obligor may reasonably expect significant changes in his or her financial situation which would permit higher payments to be made during later periods of the life of the note.

(4) Determinations made under paragraphs (e)(2) and (e)(3) of this section are intended for the benefit of the Government in reducing the amount of claim payable by VA and/or avoiding the establishment of uncollectable debts owing to the United States. Such determinations are discretionary on the part of VA and shall not constitute a defense to any legal action to terminate the loan nor vest any appellate right in an obligor which would require further review of the case. (Authority: 38 U.S.C. 501(a), 3703(c)(1))

(f) Whenever any veteran disposes of residential property securing a guaranteed or insured loan obtained by him or her under 38 U.S.C., chapter 37, and for which the commitment to make the loan was made prior to March 1, 1988, the Secretary, upon application made by such veteran, shall issue to the veteran a release relieving him or her of all further liability to the Secretary on account of such loan (including liability for any loss resulting from any default of the transferee or any subsequent purchaser of such property) if the Secretary has determined, after such investigation as may be deemed appropriate, that there has been compliance with the conditions prescribed in 38 U.S.C. 3713. The assumption of full liability for repayment of the loan by the transferee of the property must be evidenced by an agreement in writing in such form as the Secretary may require. Release of the veteran from liability to the Secretary will not impair or otherwise affect the Secretary's guaranty or insurance liability on the loan, or the liability of the veteran to the holder. Any release of liability granted to a veteran by the Secretary shall inure to the spouse of such veteran. The release of the veteran from liability to the Secretary will constitute the Secretary's prior approval to a release of the veteran from liability on the loan by the holder thereof. (Authority: 38 U.S.C. 3713)

(g) If, on or after July 1, 1972, any veteran disposes of residential property securing a guaranteed or insured loan obtained under 38 U.S.C., chapter 37, without receiving a release from liability with respect to such loan under 38 U.S.C. 3713 and a default subsequently occurs which results in liability of the veteran to the Secretary on account of the loan, the Secretary may relieve the veteran of such liability if he determines that:

(1) A transferee either immediate or remote is legally liable to the Secretary for the debt of the original veteran-borrower established after the termination of the loan, and

(2) The original loan was current at the time such transferee acquired the property, and

(3) The transferee who is liable to the Secretary is found to have been a satisfactory credit risk at the time he or she acquired the property.

(h) If a veteran or any other person disposes of residential property securing a guaranteed or insured loan for which a commitment was made on or after March 1, 1988, and the veteran or other person notifies the loan holder in writing before disposing of the property, the veteran or other person shall be relieved of all further liability to the Secretary with respect to the loan (including liability for any loss resulting from any default of the purchaser or any subsequent owner of the property) and the application for assumption shall be approved if the holder determines that:

(1) The proposed purchaser is creditworthy;

(2) The proposed purchaser is contractually obligated to assume the loan and the liability to indemnify the Department of Veterans Affairs for the amount of any claim paid under the guaranty as a result of a default on the loan, or has already done so; and,

(3) The payments on the loan are current.

Should these requirements be satisfied, the holder may also release the veteran or other person from liability on the loan. This does not apply if the approval for the assumption is granted upon special appeal to avoid immediate foreclosure. (Authority: 38 U.S.C. 3714)

§36.4324 RELEASE OF SECURITY

(a) Except upon full payment of the indebtedness the holder shall not release a lien or other right in or to real property held as security for a guaranteed or insured loan, or grant a fee or other interest in such property, without the prior approval of the Secretary, unless in the opinion of the holder such release does not involve a decrease in the value of the security in excess of $2,500: *Provided*, that the aggregate of the reduction in the original value of the security resultant from such releases without the Secretary's prior approval does not exceed $2,500.

(b) Holder may release from the lien personal property including crops without the prior approval of the Secretary.

(c) Except upon full payment of the indebtedness or upon the prior approval of the Secretary, the holder shall not release a lien under paragraph (a) or (b) of this section unless the consideration received for the release is commensurate with the fair market value of the property released and the entire consideration is applied to the indebtedness, or if encumbrance on other property is accepted in lieu of that released it shall be the holder's duty to acquire such lien on property of substantially equal value which is reasonably capable of serving the purpose for which the property released was utilized.

(d) Failure of the holder to comply with the provisions of this section shall not in itself affect the validity of the title of a purchaser to the property released.

(e) The holder shall notify the Secretary of any such release or substitution of security within 30 days after completion of such transaction.

(f) The release of the personal liability of any obligor on a guaranteed or insured obligation resultant from the act or omission of any holder without the prior approval of the Secretary shall release the obligation of the Secretary as guarantor or insurer, except when such act or omission consists of:

(1) Failure to establish the debt as a valid claim against the assets of the estate of any deceased obligor, provided no lien for the guaranteed or insured debt is thereby impaired or destroyed; or

(2) An election and appropriate prosecution of legally available effective remedies with respect to the repossession or the liquidation of the security in any case, irrespective of the identity or the survival of the original or of any subsequent debtor, if holder shall have given such notice as required by §36.4317 of this part and if, after receiving such notice, the Secretary shall have failed to notify the holder within 15 days to proceed in such manner as to effectively preserve the personal liability of the parties liable, or such of them as the Secretary indicates in such notice to the holder; or

(3) The release of an obligor, or obligors, from liability on an obligation secured by a lien on property, which release is an incident of and contemporaneous with the sale of such property to an eligible veteran who assumed such obligation, which assumed obligation is guaranteed on the assuming veteran's account pursuant to 38 U.S.C., chapter 37; or

(4) The release of an obligor or obligors as provided in §36.4314(d) of this part; or, the release of an obligor, or obligors, incident to the sale of property securing the loan which the holder is authorized to approve under the provisions of 38 U.S.C. 3714. (Authority: 38 U.S.C. 3714)

§36.4325 PARTIAL OR TOTAL LOSS OF GUARANTY OR INSURANCE

(a) Subject to the incontestable provisions of 38 U.S.C. 3721 as to loans guaranteed or insured on or subsequent to July 1, 1948, there shall be no liability on account of a guaranty or insurance, or any certificate or other evidence thereof, with respect to a transaction in which a signature to the note, the mortgage, or any other loan papers, or the application for guaranty or insurance is a forgery; or in which the certificate of discharge or the certificate of eligibility is counterfeited, or falsified, or is not issued by the Government.

(l) Except as to a holder who acquired the loan instrument before maturity, for value, and without notice, and who has not directly or by agent participated in the fraud, or in the misrepresentation hereinafter specified, any willful and material misrepresentation or fraud by the lender, or by a holder, or the agent of either, in procuring the guaranty or the insurance credit, shall relieve the Secretary of liability, or, as to loans guaranteed or insured on or subsequent to July 1, 1948, shall constitute a defense against liability on account of the guaranty or insurance of the loan in respect to which the willful misrepresentation, or the fraud, is practiced: *Provided*, That if a misrepresentation, although material, is not made willfully, or with fraudulent intent, it shall have only the consequences prescribed in paragraphs (b) and (c) of this section.

(b) In taking security required by 38 U.S.C., chapter 37 and the regulations concerning guaranty or insurance of loans to veterans, a holder shall obtain the required lien on property the title to which is such as to be acceptable to prudent lending institutions, informed buyers, title companies, and attorneys, generally, in the community in which the property is situated: *Provided*, That a title will not be unacceptable by reason of any of the limitations on the quantum or quality of the property or title stated in §36.4350(b) and if such holder fails in this respect or fails to comply with 38 U.S.C., chapter 37 and the regulations concerning guaranty or insurance of loans to veterans with respect to:

(1) Obtaining and retaining a lien of the dignity prescribed on all property upon which a lien is required by 38 U.S.C., chapter 37 or the regulations concerning guaranty or insurance of loans to veterans,

(2) Inclusion of power to substitute trustees (§36.4327),

(3) The procurement and maintenance of insurance coverage (§36.4326),

(4) Advice to Secretary as to default (§36.4315),

(5) Notice of intention to begin action (§36.4317),

(6) Notice to the Secretary in any suit or action, or notice of sale (§36.4319),

(7) The release, conveyance, substitution, or exchange of security (§36.4324),

(8) Lack of legal capacity of a party to the transaction incident to which the guaranty or the insurance is granted (§36.4328),

(9) Failure of the lender to see that any escrowed or earmarked account is expended in accordance with the agreement,

(10) The taking into consideration of limitations upon the quantum or quality of the estate or property (§36.4350(b)),

(11) Any other requirement of 38 U.S.C., chapter 37 or the regulations concerning guaranty or insurance of loans to veterans which does not by the terms of said chapter or the regulations concerning guaranty or insurance of loans to veterans result in relieving the Secretary of all liability with respect to the loan,

no claim on the guaranty or insurance shall be paid on account of the loan with respect to which such failure occurred, or in respect to which an unwillful misrepresentation occurred, until the amount by which the ultimate liability of the Secretary would thereby be increased has been ascertained. The burden of proof shall be upon the holder to establish that no increase of ultimate liability is attributable to such failure or misrepresentation. The amount of increased liability of the Secretary shall be offset by deduction from the amount of the guaranty or insurance otherwise payable, or if consequent upon loss of security shall be offset by crediting to the indebtedness the amount of the impairment as proceeds of the sale of security in the final accounting to the Secretary. To the extent the loss resultant from the failure or misrepresentation prejudices the Secretary's right of subrogation acceptance by the holder of the guaranty or insurance payment shall subordinate the holder's right to those of the Secretary.

(c) If after the payment of a guaranty or an insurance loss, or after a loan is transferred pursuant to §36.4318(a), the fraud, misrepresentation or failure to comply with the regulations in this subpart as provided in this section is discovered and the Secretary determines that an increased loss to the Government resulted therefrom, the transferor or person to whom such payment was made shall be liable to the Secretary for the amount of the loss caused by such misrepresentation or failure.

§36.4326 HAZARD INSURANCE

The holder shall require insurance policies to be procured and maintained in an amount sufficient to protect the security against the risks or hazards to which it may be subjected to the extent customary in the locality. Flood insurance will be required in respect to any loan closed on and after March 2, 1974, if the security is located in an area identified by the Secretary of Housing and Urban Development as having special flood hazards and in which the sale of flood insurance is available under the National Flood Insurance Program. The amount of flood insurance required will be equal to the outstanding balance of the loan or the maximum limit of coverage available for the particular type of property under the national flood insurance program, whichever is less. All moneys received under such policies covering payment of insured losses shall be applied to restoration of the security or to the loan balance.

§36.4327 SUBSTITUTION OF TRUSTEES

In jurisdictions in which valid, any deed of trust or mortgage securing a guaranteed or insured loan, if it names trustees, or confers a power of sale otherwise, shall contain a provision empowering any holder of the indebtedness to appoint substitute trustees, or other person with such power to sell, who shall succeed to all the rights, powers, and duties of the trustees, or other person, originally designated.

§36.4328 CAPACITY OF PARTIES TO CONTRACT

Nothing in §§36.4300 to 36.4375, inclusive, shall be construed to relieve any lender of responsibility otherwise existing, for any loss caused by the lack of legal capacity of

any person to contract, convey, or encumber, or caused by the existence of other legal disability or defects invalidating, or rendering unenforceable in whole or in part, either the loan obligation or the security therefor.

§36.4329 GEOGRAPHICAL LIMITS

Any real property purchased, constructed, altered, improved, or repaired with the proceeds of a guaranteed or insured loan shall be situated within the United States which for purposes of 38 U.S.C., chapter 37 is here defined as the several States, Territories and possessions, and the District of Columbia, the Commonwealth of Puerto Rico, and the Commonwealth of the Northern Mariana Islands.

§36.4330 MAINTENANCE OF RECORDS

(a) The holder shall maintain a record of the amounts of payments received on the obligation and disbursements chargeable thereto and the dates thereof. This record shall be maintained until the Secretary ceases to be liable as guarantor or insurer of the loan. For the purpose of any accounting with the Secretary or computation of a claim any holder who fails to maintain such record shall be presumed to have received on the dates due all sums which by the terms of the contract are payable prior to date of claim for default, and the burden of going forward with evidence and of ultimate proof of the contrary shall be on such holder.

(b) The lender shall retain copies of all loan origination records on a VA guaranteed loan for at least one year from the date of loan closing. Loan origination records include the loan application, including any preliminary application, verifications of employment and deposit, all credit reports, including preliminary credit reports, copies of each sales contract and addendums, letters of explanation for adverse credit items, discrepancies and the like, direct references from creditors, correspondence with employers, appraisal and compliance inspection reports, reports on termite and other inspections of the property, builder change orders, and all closing papers and documents. (Authority: 38 U.S.C. 501(a), 3703(c)(1))

(c) The Secretary has the right to inspect, examine, or audit, at a reasonable time and place, the records or accounts of a holder pertaining to loans guaranteed or insured by the Secretary.

§36.4332 DELIVERY OF NOTICE

Any notice required by §§36.4300 to 36.4375 to be given the Secretary must be in writing or such communications medium as may be approved by an official designated in §36.4342 and delivered, by mail or otherwise, to the VA office at which the guaranty or insurance was issued, or to any changed address of which the holder has been given notice. Such notice must plainly identify the case by setting forth the name of the original veteran obligor and the file number assigned to the case by the Secretary, if available, or otherwise the name and serial number of the veteran. If mailed, the notice shall be by certified mail when so provided by §§36.4300 to 36.4375. This paragraph does not apply to legal process.

§36.4333 SATISFACTION OF INDEBTEDNESS

Upon full satisfaction of a guaranteed loan by payment or otherwise it shall be the duty of the holder to cancel the endorsement, if any, of the Secretary; and forthwith inform the Secretary of such cancellation. In the event the Secretary's liability thereon is evidenced by an instrument separate from the instrument evidencing the debtor's

obligation, the instrument evidencing the obligation of the Secretary shall be returned to the Department of Veterans Affairs office issuing same, or to the Central Office, with the holder's cancellation or endorsement of release thereon.

§36.4334 INCORPORATION BY REFERENCE

Regulations issued under 38 U.S.C. Chapter 37, and in effect on the date of any loan which is submitted and accepted or approved for a guaranty or for insurance thereunder, shall govern the rights, duties, and liabilities of the parties to such loan and any provisions of the loan instruments inconsistent with such regulations are hereby amended and supplemented to conform thereto.

§36.4335 SUPPLEMENTARY ADMINISTRATIVE ACTION

Notwithstanding any requirement, condition, or limitation stated in or imposed by the regulations concerning the guaranty or insurance of loans to veterans, the Chief Benefits Director, or the Director, Loan Guaranty Service, within the limitations and conditions prescribed by the Secretary, is hereby authorized, if he or she finds the interests of the Government are not adversely affected, to relieve undue prejudice to a debtor, holder, or other person, which might otherwise result, provided no such action may be taken which would impair the vested rights of any person affected thereby. If such requirement, condition, or limitation is of an administrative or procedural (not substantive) nature, any employee designated in §36.4342 is hereby authorized to grant similar relief if he or she finds the failure or error of the lender was due to misunderstanding or mistake and that the interests of the Government are not adversely affected. Provisions of the regulations considered to be of an administrative or procedural (nonsubstantive) nature are limited to the following:

(a) The requirement in §36.4303(a) that a lender of a class described under 38 U.S.C. 3702(d) originating a loan under the automatic (nonprior approval) procedure report such loan for issuance of guaranty or insurance evidence within 60 days following full disbursement. Waiver of the lender's failure to report the loan within the 60-day period shall be confined to cases where the loan is not in default.

(b) The requirement in §36.4303(d) that a lender originating a loan under a certificate of commitment report the loan for issuance of guaranty or insurance evidence within 60 days following actual payment of the full proceeds of the loan. In such cases it is not necessary that a finding be made that the loan is not in default.

(c) The requirement in §36.4314(e) that a holder promptly forward an advice of the terms of any agreement effecting a reamortization or extension of a loan.

(d) The 45-day requirement in §36.4315(a) concerning the giving of notice of default.

(e) The requirement in §36.4317 that a holder give 30 days advance notice of its intention to foreclose.

(f) The requirement in §36.4317(b) that a holder give notice of repossession of personal property within 10 days after such repossession has occurred.

(g) The requirement in §36.4307(a) that a lender obtain the prior approval of the Secretary before closing a joint loan if the lender or class of lenders is eligible or has

been approved by the Secretary to close loans on the automatic basis pursuant to 38 U.S.C. 3702(d). (Authority: 38 U.S.C. 3703(c)(1))

(h) The requirements in §36.4303(k) of this part concerning the giving of notice in assumption cases under 38 U.S.C. 3714. (Authority: 38 U.S.C. 3714 and 3720)

§36.4336 ELIGIBILITY OF LOANS; REASONABLE VALUE REQUIREMENTS

(a) Evidence of guaranty or insurance shall be issued in respect to a loan for any of the purposes specified in 38 U.S.C. 3710(a) only if:

(1) The proceeds of such loan have been used to pay for the property purchased, constructed, repaired, refinanced, altered, or improved and;

(2) (i) Except as to refinancing loans pursuant to 38 U.S.C. 3710(a)(8) or (9)(B)(i), the loan including any scheduled deferred interest added to principal, does not exceed the reasonable value of the property or projected reasonable value of a new home which is security for a graduated payment mortgage loan, as appropriate, as determined by the Secretary, and

(ii) For the purpose of determining the reasonable value of a graduated payment mortgage loan to purchase a new home, the reasonable value of the property as of the time the loan is made shall be calculated to increase at a rate not in excess of 2.5 percent per year, but in no event may the projected value of the property exceed 115 percent of the initially established reasonable value, and (Authority: 38 U.S.C. 3703(d)(2))

(3) The veteran has certified, in such form as the Secretary may prescribe, that the veteran has paid in cash from his or her own resources on account of such purchase, construction, alteration, repair, or improvement a sum equal to the difference, if any, between the purchase price or cost of the property and its reasonable value.

(b) Notwithstanding that the aggregate of the loan amount in the case of loans for the purposes specified in paragraph (a) of this section, and the amount remaining unpaid on taxes, special assessments, prior mortgage indebtedness, or other obligations of any character secured by enforceable superior liens or a right to such lien existing as of the date the loan is closed exceeds the reasonable value of such property as of said date and that evidence of guaranty or insurance credit is issued in respect thereof, as between the holder and Secretary (for the purpose of computing the claim on the guaranty or insurance and for the purposes of §36.4320, and all accountings), the indebtedness which is the subject of the guaranty or insurance shall be deemed to have been reduced as of the date of the loan by a sum equal to such excess, less any amounts secured by liens released or paid on the obligations secured by such superior liens or rights by a holder or others without expense to or obligation on the debtor resulting from such payment, or release of lien or right; and all payments made on the loan shall be applied to the indebtedness as so reduced. Nothing in this paragraph affects any right or liability resulting from fraud or willful misrepresentation. (Authority: 38 U.S.C. 501(a), 3703(c)(1); 38 U.S.C. 501(a), 3710, 3712)

Underwriting Standards, Processing Procedures, and Lender Responsibility and Certification

§36.4337 UNDERWRITING STANDARDS, PROCESSING PROCEDURES, LENDER RESPONSIBILITY AND LENDER CERTIFICATION

(a) Except for refinancing loans guaranteed pursuant to 38 U.S.C. 3710(a)(8), the standards contained in paragraph (b) of this section will be used to determine that the veteran's present and anticipated income and expenses, and credit history are satisfactory.

(b) *Methods*. There are two primary underwriting tools that will be used in determining the adequacy of the veteran's present and anticipated income. They are: debt-to-income ratio and residual income. Each is described in paragraphs (c) and (d) of this section respectively. Ordinarily, in order to qualify for a loan, the veteran must meet both standards. Failure to meet one standard, however, will not automatically disqualify a veteran. The following shall apply to cases where a veteran does not meet both standards:

(1) If the debt-to-income ratio is 41 percent of less, and the veteran does not meet the residual income standard, the loan may be approved with justification, by the underwriter's supervisor, as set out in paragraph (b)(4) of this section.

(2) If the debt-to-income ratio is greater than 41 percent, (unless it is larger due solely to the existence of tax-free income which should be noted in the loan file) the loan may be approved with justification, by the underwriter's supervisor, as set out in paragraph (b)(4) of this section.

(3) If the ratio is greater than 41 percent and the residual income exceeds the guidelines by at least 20 percent the second level review and statement of justification is not required.

(4) In any case described by paragraphs (b)(1) and (b)(2) of this section, the lender must fully justify the decision to approve the loan or submit the loan to the Secretary for prior approval in writing. The lender's statement must not be perfunctory, but should address the specific compensating factors, as set forth in (b)(5), of this section, justifying the approval or submission of the loan. The statement must be signed by the underwriter's supervisor. It must be stressed that the statute requires not only consideration of a veteran's present and anticipated income and expenses, but also that the veteran be a satisfactory credit risk. Therefore, meeting both the debt-to-income ratio and residual income standards does not mean the loan is automatically approved. It is the lender's responsibility to base the loan approval or disapproval on all the factors present for any individual veteran. The veteran's credit must be evaluated based on criteria set forth in paragraph (c) of this section as well as a variety of compensating factors that should be evaluated.

(5) The following are examples of acceptable compensating factors to be considered in the course of underwriting a loan:

(i) Excellent long-term credit;
(ii) Conservative use of consumer credit;
(iii) Minimal consumer debt;
(iv) Long-term employment;
(v) Significant liquid assets;
(vi) Down payment or the existence of equity in refinancing loans;
(vii) Little or no increase in shelter expense;
(viii) Military benefits;
(ix) Satisfactory homeownership experience;
(x) High residual income; and
(xi) Low debt-to-income ratio.

This list is not exhaustive and the items are not in any priority order. Valid compensating factors should represent unusual strengths rather that mere satisfaction of basic program requirements. Compensating factors must be relevant to the marginality of weakness.

(c) *Debt-to-income ratio*. A debt-to-income ratio that compares the veteran's anticipated monthly housing expense and total monthly obligations to his or her stable monthly income will be computed to assist in the assessment of the potential risk of the loan. The ratio will be determined by taking the sum of the monthly Principal, Interest, Taxes and Insurance (PITI) to the loan being applied for, homeowners and other assessments such as special assessments, condominium fees, homeowners association fees, etc., and any long-term obligations divided by the total of gross salary or earnings and other compensation or income. The ratio should be rounded to the nearest two digits; i.e., 35.6 percent would be rounded to 36 percent. The standard is 41 percent or less. If the ratio is greater than 41 percent (unless it is larger due solely to the existence of tax free income which should be noted in the loan file) the steps cited in paragraphs (b)(1) through (b)(5) of this section apply.

(d) *Residual income*.

(1) The guidelines provided in this subparagraph for residual income will be used to determine whether the veteran's monthly residual income will be adequate to meet living expenses after estimated monthly shelter expenses have been paid and other monthly obligations have been met. The guidelines for residual income are based on data supplied in the Consumer Expenditure Survey (CES) published by the Department of Labor's Bureau of Labor Statistics. Regional minimum incomes have been developed for loan amounts up to $69,999 and for loan amounts of $70,000 and above. It is recognized that the purchase price of the property may affect family expenditure levels in individual cases. This factor may be given consideration in the final determination in individual loan analyses. For example, a family purchasing in a higher-priced neighborhood may feel a need to incur higher than average expenses to support a lifestyle comparable to that in their environment, whereas a substantially lower-priced home purchase may not compel such expenditures. It should also be clearly understood from this information that no single factor is a final determinant in any applicant's qualification for a VA guaranteed loan. Once the residual income has been established, other important factors must be examined. One such consideration is the amount being paid currently for rental or housing expenses. If the proposed shelter expense is materially in excess of what is currently being paid, the case may required closer scrutiny. In such cases, consideration should be given to the ability of the borrower and spouse to accumulate liquid assets, i.e., cash and bonds, and to the amount of debts incurred while paying a lesser amount for shelter. For example, if an application allows little or no capital reserves and excessive obligations, it may not be reasonable to conclude that a substantial increase in shelter expenses can be absorbed. Another factor of prime importance is the applicant's manner of meeting obligations. A poor credit history alone is a basis for disapproving a loan, as is an obviously inadequate income. When one or the other is marginal, however, the remaining aspect must be closely examined to assure that the loan applied for will not exceed the applicant's ability or capacity to repay. Therefore, it is important to remember that the figures provided below for residual income are to be used as a guide and should be used in conjunction with the steps outlined in paragraphs (b)(1) through (b)(6) of this section. The residual income guidelines are as follows:

(i) Table of residual incomes by region (for loan amounts of $69,999 and below):

Table of Residual Incomes by Region

[For loan amounts of $69,999 and below]

Family Size[1]	Northeast	Midwest	South	West
1	$348	$340	$340	$379
2	583	570	570	635
3	702	687	687	765
4	791	773	773	861
5	821	803	803	894

1. For families with more than five members, add $70 for each additional member up to a family of seven.

(ii) Table of residual income by region (for loan amounts of $70,000 and above):

Table of Residual Incomes by Region
[For loan amounts of $70,000 and above]

Family Size[1]	Northeast	Midwest	South	West
1	$401	$393	$393	$437
2	673	658	658	733
3	810	792	792	882
4	913	893	893	995
5	946	925	925	1,031

1. For families with more than five members, add $70 for each additional member up to a family of seven.

(iii) *Geographic regions for residual income guidelines*: Northeast--Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont; Midwest--Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin; South--Alabama, Arkansas, Delaware, District of Columbia, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, Oklahoma, Puerto Rico, South Carolina, Tennessee, Texas, Virginia, and West Virginia; West-- Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming.

(iv) *Military adjustments*: For loan applications in which either the borrower or the spouse is an active-duty serviceperson, the residual income figures will be reduced by a minimum of 5 percent if there is a clear indication that the borrower or spouse will continue to receive the benefits resulting from the use of facilities on a nearby military base. (This reduction applies to tables in paragraphs (d)(1)(i) and (d)(1)(ii) of this section.)

(2) *Income*. Only stable and reliable income of the veteran and spouse can be considered in determining ability to meet mortgage payments. Income can be considered

stable and reliable if it can be concluded that it will continue during the foreseeable future.

(i) *Verification*. Income of the borrower and spouse which is derived from employment and which is considered in determining the family's ability to meet the mortgage payments, payments on debts and other obligations, and other expenses, must be verified if the spouse is employed and will be contractually obligated on the loan, the combined income of both the veteran and spouse is considered when the income of the veteran alone is not sufficient to qualify for the amount of the loan sought. In other than community property States, if the spouse will not be contractually obligated on the loan, Regulation B, promulgated by the Federal Reserve Board pursuant to the Equal Credit Opportunity Act prohibits any request for, or consideration of information concerning the spouse (including income, employment, assets, or liabilities), except that if the applicant is relying on alimony, child support, or maintenance payments from a spouse or former spouse as a basis for repayment of the loan, information concerning such spouse or former spouse may be requested and considered (see paragraph (d)(3)(iii) of this section). In community property States, information concerning a spouse may be requested and considered in the same manner as that for the applicant. The standards applied to income of the veteran are also applicable to that of the spouse. There can be no discounting of income on account of sex, marital status, or any other basis prohibited by the Equal Credit Opportunity Act. Income claimed by an applicant that is not or cannot be verified cannot be given consideration when analyzing the loan. If the veteran or spouse has been employed by a present employer for less than 2-years, a 2-year history covering prior employment, schooling or other training must be secured. Any periods of unemployment must be explained. Employment verifications must be no more than 90 days old to be considered valid. For loans closed automatically, this requirement will be considered satisfied if the date of the employment verification is within 90 days of the date of the veteran's application to the lender.

(ii) *Income Reliability*. Income received by the borrower and spouse is to be used only if it can be concluded that the income will continue during the foreseeable future and thus should be properly considered in determining ability to meet the mortgage payments. There can be no discounting of income solely because it is derived from an annuity, pension or other retirement benefit, or from part-time employment. However, unless income from overtime work and part-time or second jobs can be accorded a reasonable likelihood that it is continuous and will continue in the foreseeable future, such income should not be used. The hours of duty and other work conditions of the applicant's primary job, and the period of time in which the applicant was employed under such arrangement must be such as to permit a clear conclusion as to a good probability that overtime or part-time or secondary employment can and will continue. Income from overtime work and part-time jobs not eligible for inclusion as primary income, may, if properly verified, be used to offset the payments due on debts and obligations of a relatively short term. Such income must be described in the loan file. The amount of any pension or compensation and other income such as dividends from stocks, interest from bonds, savings accounts, or other deposits, rents, royalties, etc., will be used as primary income if it is reasonable to conclude that such income will continue in the foreseeable future. Otherwise, it may be used only to offset short-term debts, as above. Certain military allowances, as to which likely duration cannot be determined, will also be used only to offset short-term obligations. Such allowances are: pro-pay, flight or hazard pay, and overseas or combat pay, all of which are subject to periodic review and/or testing of the recipient to ascertain whether eligibility for such pay will continue. Only if it can be shown that such pay has continued for a prolonged period and can be expected to continue because of the nature of the recipient's assigned duties, will such income be considered as primary income. For instance, flight pay verified for a

pilot can be regarded as probably continuous and thus should be added to the base pay. Income derived from service in the reserves or National Guard may be used if the applicant has served in such capacity for a period of time sufficient to evidence good probability that such income will continue. The total period of active and reserve service may be helpful in this regard. Otherwise, such income may be used to offset short-term debts. There are a number of additional income sources whose contingent nature precludes their being considered as available for repayment of a long-term mortgage obligation. Temporary income items such as VA educational allowances and unemployment compensation do not represent stable and reliable income and will not be taken into consideration in determining the ability of the veteran to meet the income requirement of the governing law. As required by the Equal Opportunity Act Amendments of 1976, Public Law 94-239, income from public assistance programs is used to qualify a loan if it can be determined that the income will probably continue for a substantial fraction of the term of the loan; i.e., one-third or more. For instance, aid to dependent children being received for a 5-year old child that will continue until the child achieves majority would be used to qualify for a 30-year loan.

(iii) *Alimony, child support, maintenance payments*. If an applicant chooses to reveal income from alimony, child support, or maintenance payments (after first having been informed that any such disclosure is voluntary pursuant to the Federal Reserve Board's Regulation B) such payments are considered as income to the extent that the payments are likely to be considered made. Factors to be considered in determining the likelihood of consistent payments include, but are not limited to: Whether the payments are received pursuant to a written agreement or court decree; the length of time the payments have been received; the regularity of receipt; the availability of procedures to compel payment; and the creditworthiness of the payor, including credit history of the payor when available under the Fair Credit Reporting Act or other applicable laws. However, the Fair Credit Reporting Act (15 U.S.C. 1681b) limits the permissible purposes for which credit reports may be ordered, in the absence of written instructions of the consumer to whom the report relates, to business transactions involving the subject of the credit report or extensions of credit to the subject of the credit report.

(iv) *Military quarters allowance*. With respect to off-base housing (quarters) allowances for service personnel on active duty, it is the policy of the Department of Defense (DoD) to utilize available on-base housing when possible. In order for a quarters allowances to be considered as continuing income, it is necessary that the applicant furnish written authorization from his or her commanding officer for off-base housing. This authorization should verify that quarters will not be made available and that the individual should make permanent arrangements for nonmilitary housing. DD Form 1747, Status of Housing Availability, is used by the Family Housing Office to advise personnel regarding family housing. Unless conditions of item (e) or (f) of DD Form 1747 apply, the applicant's quarters allowance cannot be considered. Of course, if the applicant's income less quarters allowance is sufficient, there is no need for assurance that the applicant has permission to occupy nonmilitary housing provided that a determination can be made that the occupancy requirements of the law will be met. Also, authorization to obtain off-base housing will not be required when certain duty assignments would clearly qualify service personnel with families for quarters allowance. For instance, off-base housing authorizations need not be obtained for service personnel stationed overseas who are not accompanied by their families, recruiters on detached duty, or military personnel stationed in areas where no on-base housing exists. In any case in which no off-base housing authorization is obtained, an explanation of the circumstances justifying its omission must be included with the loan application except when it has been established by the VA facility of jurisdiction that the waiting lists for off-base housing are so long that is improbable that individuals desiring to purchase off-

base housing would be precluded from doing so in the foreseeable future. If stations make such a determination, a release shall be issued to inform lenders.

(v) *Commissions*. When all or a major portion of the veteran's income is derived from commissions, it will be necessary to establish the stability of such income if it is to be considered in the loan analysis for the repayment of the mortgage debt and/or short-term obligations. In order to assess the value of such income, lenders should obtain written verification of the actual amount of commissions paid to date, the basis for the payment of such commissions and when commissions are paid; i.e., monthly, quarterly, semiannually, or annually. The length of the veteran's employment in this type of occupation is also an important factor in the assessment of the stability of the income. If the veteran has been employed for a relatively short time, the income should not normally be considered stable unless the product or service was the same or closely related to the product or service sold in an immediate prior position.

(vi) *Self-employment*. When a self-employed applicant has been in the business a relatively short period of time (i.e., less that 2 years), sufficient information must be obtained to ascertain that the applicant has the training, experience and other qualifications necessary to be successful in the enterprise. For any self-employed person, verification of the amount of income is accomplished by obtaining a profit and loss statement for the prior fiscal year (12-month accounting cycle), plus the period year to date since the end of the last fiscal year (or for whatever shorter period records may be available), and a current balance sheet showing all assets and liabilities. The profit and loss statement and balance sheet will be prepared by an accountant based on the financial records. In some cases the nature of the business or the content of the financial statement may necessitate an independent audit certified as accurate by the accountant. Depending on the situation, this data may be on the veteran and/or the business. When it is otherwise not possible to determine a self-employed applicant's qualification from an income standpoint, the applicant may wish to voluntarily offer to submit copies of complete income tax returns, including all schedules for the past 2 years, or for whatever additional period is deemed necessary to properly demonstrate a satisfactory earning record. Depreciation claimed as a deduction on the tax return or financial record of the business may be added in as net income. If the business is a corporation or partnership, a list of all stockholders or partners showing the interest each holds in the business will be required. Some cases may justify a written credit report on the business as well as the applicant. When the business is of an unusual type and it is difficult to determine the probability of its continued operation, explanations as to the function and purpose of the business may be needed from the applicant and/or any other qualified party with the acknowledged expertise to express a valid opinion.

(vii) *Recently discharged veterans*. Loan applications received from recently discharged veterans who have little or no employment experience other than military occupation and from veterans seeking VA guaranteed loans who have retired after 20 years of active military duty require special attention. The retirement income of the latter veterans in many cases may not be sufficient to meet the statutory income requirements for the loan amount sought. Many have obtained full-time employment and have been employed in their new jobs for a very short time.

(A) It is essential in determining whether veterans in these categories qualify from the income standpoint for the amount of the loan sought, that the facts in respect to their present employment and retirement income be fully developed, and that each case be considered on its individual merits.

(B) In most cases the veteran's current income or current income plus his or her retirement income is sufficient. The problem lies in determining whether it can be properly concluded that such income level will continue for the foreseeable future. If the veteran's employment status is that of a trainee or apprentice, this will, of course, be a factor. In cases of the self-employed, the question to be resolved is whether there are reasonable prospects that the business enterprise will be successful and produce the required income. Unless a favorable conclusion can be made, the income from such source should not be considered in the loan analysis.

(C) If a recently discharged veteran has no prior employment history and the veteran's verification of employment shows he or she has not been on the job a sufficient time in which to become established, consideration should be given to the duties the veteran performed in the military service. When it can be determined that the duties a veteran performed in the service are similar or are in direct relation to the duties of the applicant's present position, such duties may be construed as adding weight to his or her present employment experience and the income from the veteran's present employment thus may be considered available for qualifying the loan, notwithstanding the fact that the applicant has been on the present job only a short time. The same principle may be applied to veterans recently retired from the service. In addition, when the veteran's income from retirement, in relation to the total of the estimated shelter expense, long-term debts and amount available for family support, is such that only minimal income from employment is necessary to quality from the income standpoint, it would be proper to resolve the doubt in favor of the veteran. It would be erroneous, however, to give consideration to a veteran's income from employment for a short duration in a job requiring skills for which the applicant has had no training or experience.

(D) To illustrate the foregoing, it would be proper to use short-term employment income in qualifying a veteran who had experience as an airplane mechanic in the military service and the individual's employment after discharge or retirement from the service is in the same or allied fields; e.g., auto mechanic or machinist. This presumes, however, that the verification of employment included a statement that the veteran was performing the duties of the job satisfactorily, the possibility of continued employment was favorable and that the loan application is eligible in all other respects. An example of non-qualifying experience is that of a veteran who was an Air Force pilot and has been employed in insurance sales on commission for a short time. Most cases, of course, fall somewhere between those extremes. It is for this reason that the facts of each case must be fully developed prior to closing the loan automatically or submitting the case to VA for prior approval.

(viii) *Employment of short duration*. The provisions of paragraph (d)(2)(vii) of this section are similarly applicable to applicants whose employment is of short duration. Such cases will entail careful consideration of the employer's confirmation of employment, probability of permanency, past employment record, the applicant's qualifications for the position, and previous training, including that received in the military service. In the event that such considerations do not enable a determination that the income from the veteran's current position has a reasonable likelihood of continuance, such income should not be considered in the analysis. Applications received from persons employed in the building trades, or in other occupations affected by climatic conditions, should be supported by documentation evidencing the applicant's total earnings to date and covering a period of not less that 1 year. If the applicant works out of a union, evidence of the previous year's earnings should be obtained together with a verification of employment from the current employer.

(xi) *Rental income*.

(A) *Multi-unit Subject Property*. When the loan pertains to a structure with more that a one-family dwelling unit, the prospective rental income will not be considered unless the veteran can demonstrate a reasonable likelihood of success as a landlord, and sufficient cash reserves are verified to enable the veteran to carry the mortgage loan payments (principal, interest, taxes, and insurance) without assistance from the rental income for a period of at least 6 months. The determination of the veteran's likelihood of success as a landlord will be based on documentation prior experience in managing rental units, or other collection activities. The amount of rental income to be used in the loan analysis will be based on the prior rental history of the units as verified by the seller's financial records (e.g., prior years' tax returns) for existing structures or, for proposed construction, the appraiser's opinion of the property's fair monthly rental. Adjustments will be applied to reduce estimated gross rental income by proper allowances for operating expenses and vacancy losses.

(B) *Rental of Existing Home*. Proposed rental of a veteran's existing property may be used to offset the mortgage payment on that property, provided there is no indication that the property will be difficult to rent. If available, a copy of the rental agreement should be obtained. It is the responsibility of the loan underwriter to be aware of the condition of the local rental market. For instance, in areas where the rental market is very strong the absence of a lease should not automatically prohibit the offset of the mortgage by the proposed rental income.

(C) *Other Rental Property*. If income from rental property will be used to qualify for the new loan, the documentation required of a self-employed applicant should be obtained together with evidence of cash reserves equaling 3 months PITI on the rental property. As for any self-employed earnings (see paragraph (d)(3)(vi) of this section), depreciation claimed may be added back in as income. In the case of a veteran who has no experience as a landlord, it is unlikely that the income from a rental property may be used to qualify for the new loan.

(x) *Taxes and other deductions*. Deductions to be applied for Federal income taxes and Social Security may be obtained from the Employer's Tax Guide (Circular E) issued by the Internal Revenue Service (IRS). (For veterans receiving a mortgage credit certificate (MCC), see paragraph (D)(3)(xi) of this section.) Any State or local taxes should be estimated or obtained from charts similar to those provided by IRS which may be available in those States with withholding taxes. A determination of the amount paid or withheld for retirement purposes should be made and used when calculating deductions from gross income. In determining whether a veteran-applicant meets the income criteria for a loan, some consideration may be given to the potential tax benefits the veteran will realize if the loan is approved. This can be done by using the instructions and worksheet portion of IRS Form W-4, Employee's Withholding Allowance Certificate, to compute the total number of permissible withholding allowances. That number can then be used when referring to IRS Circular E and any appropriate similar State withholding charts to arrive at the amount of Federal and State income tax to be deducted from gross income.

(xi) *Mortgage credit certificates*.

(A) The Internal Revenue Code, as amended by the Tax Reform Act of 1984, allows States and other political subdivisions to trade in all or part of their authority to issue mortgage revenue bonds for authority to issue MCC's. Veterans who are recipients of MCC's may realize a significant reduction in their income tax liability by receiving a

Federal tax credit for a percentage of their mortgage interest payment on debt incurred on or after January 1, 1985.

(B) Lenders must provide a copy of the MCC to VA with the home loan application. The MCC will specify the rate of credit allowed and the amount of certified indebtedness; i.e., the indebtedness incurred by the veteran to acquire a principal residence or as a qualified home improvement or rehabilitation loan.

(C) For credit underwriting purposes, the amount of tax credit allowed to a veteran under MCC will be treated as a reduction in the monthly Federal income tax. For example, a veteran having a $600 monthly interest payment and an MCC providing a 30-percent tax credit would receive a $180 (30% x $600) tax credit each month. However, because the annual tax credit, which amounts to $2,160 (12 x $180), exceeds $2,000 and is based on a 30-percent credit rate, the maximum tax credit the veteran can receive is limited to $2,000 per year (Pub. L. 98-369) or $167 per month ($2,000/12). As a consequence of the tax credit, the interest on which a deduction can be taken will be reduced to the amount of the tax credit to $433 ($600 - $167). This reduction should also be reflected when calculating Federal income tax.

(D) For underwriting purposes, the amount of the tax credit is limited to the amount of the veteran's maximum tax liability. If, in the above example, the veteran's tax liability for the year were only $1,500, the monthly tax credit would be limited to $125 (1,500/12).

(E) *Credit*. The conclusion reached as to whether or not the borrower and spouse are satisfactory credit risks must also be based on a careful analysis of the available credit data. Regulation B (Equal Credit Opportunity Act) requires that lender include, in evaluating creditworthiness on a veteran's request, the credit history, when available, of any account reported in the name of the veteran's spouse or former spouse which the veteran can demonstrate reflects accurately the veteran's willingness or ability to repay.

(1) *Adverse data*. If the analysis develops any derogatory credit information and, despite such facts, it is determined that the borrower and spouse are satisfactory credit risks, the basis for the decision must be explained. If a borrower and spouse have debts outstanding which have not been paid timely, or which they have refused to pay, the fact that the outstanding debts are paid after the acceptability of the credit is questioned or in anticipation of applying for new credit does not, of course, alter the fact that the record for paying debts has been unsatisfactory. With respect to unpaid debts, lenders may take into consideration a veteran's claim of bona fide or legal defenses. This is not applicable when the debt has been reduced to judgment.

(2) *Prior VA loans*. When the veteran's certificate of eligibility, or loan application, or other information available to the lender indicates use of VA guaranteed loan entitlement in connection with a prior loan, the lender to which the veteran is currently applying for an additional loan is on notice that VA loan experience with the applicant is an element to be considered. Such experience, especially if it is recent, may be so unfavorable that further credit is not warranted. Since credit experience with veterans' guaranteed or insured loans may not be reported by lenders to credit agencies, credit reports obtained in connection with the evaluation of subsequent loan may be deficient to that extent. Therefore, lenders processing loans on an automatic basis should develop evidence through the originator or holder of the previous loan(s) on the status and experience of such loan(s). If information cannot be obtained, lenders may contact the VA regional office through which the loan(s) was obtained. Failure to do so will

subject the lender to the risk of a possible determination by VA that when all the facts and circumstances that were readily available are considered, the conclusion of the lender relative to compliance with 38 U.S.C. 3710(b)(3) ought not be recognized as reasonable and proper and that the loan should be considered ineligible for guaranty.

(3) *Bankruptcy*. When the credit information shows that the borrower or spouse has been discharged in bankruptcy under the "straight" liquidation and discharge provisions of the bankruptcy law, this would not in itself disqualify the loan. However, in such cases it is necessary to develop complete information as to the facts and circumstances concerning the bankruptcy. Generally speaking, when the borrower or spouse, as the case may be, has been regularly employed (not self-employed) and has been discharged in bankruptcy within the last 2 or 3 years, it probably would not be possible to determine that the borrower or spouse is a satisfactory credit risk unless both of the following requirements are satisfied:

(i) The borrower or spouse has obtained consumer items on credit subsequent to the bankruptcy and has met the payments on these obligations in a satisfactory manner over a continued period, and

(ii) The bankruptcy was caused by circumstances beyond control of the borrower or spouse, e.g., unemployment, prolonged strikes, medical bills not covered by insurance. The circumstances alleged must be verified. If a borrower or spouse is self-employed, has been adjudicated bankrupt, and subsequently obtains a permanent position, a finding as to satisfactory credit risks may be made provided there is no derogatory credit information prior to self-employment, there is no evidence of derogatory credit information subsequent to the bankruptcy, and the failure of the business was not due to misconduct. A bankruptcy discharged more than 5 years ago may be disregarded. A bankruptcy discharged between 3 and 5 years ago may be given some consideration, depending upon the circumstances of the bankruptcy, and submission of evidence that the veteran has been paying his or her obligations in a timely manner.

(4) *Petition under Chapter 13 of Bankruptcy Law*. A wage earner's petition under chapter 13 of the Bankruptcy Law filed by the borrower or spouse is indicative of an effort to pay their creditors. Some plans may provide for full payment of debts while others arrange for payment of scaled down debts. Regular payments are made to a court-appointed trustee over a 2- to 3-year period (or up to 5 years in some cases). When the borrowers have made all payments in a satisfactory manner, they may be considered as having reestablished satisfactory credit. When they apply for a home loan before completion of the payout period, favorable consideration may nevertheless be given if at least three-fourths of the payments have been made satisfactorily and the Trustee or Bankruptcy Judge (Referee) approves of the new credit.

(5) *Absence of credit history*. The fact that recently discharged veterans may have had no opportunity to develop a credit history will not preclude a determination of satisfactory credit. Similarly, other loan applicants may not have established credit histories as a result of a preference for purchasing consumer items with cash rather than credit. There are also cases in which individuals may be genuinely wary of acquiring new obligations following bankruptcy, consumer credit counseling (debt proration), or other disruptive credit occurrence. The absence of the credit history in these cases will not generally be viewed as an adverse factor in credit underwriting. However, before a favorable decision is made for cases involving bankruptcies or other derogatory credit factors, efforts should be made to develop evidence of timely payment of non-installment debts such as rent and utilities. It is anticipated that this special consideration in the

absence of a credit history following bankruptcy would be the rare case and generally confined to bankruptcies which occurred over 3 years ago.

(6) *Long-term v. Short-term-debts*. All known debts and obligations including any alimony and/or child support payments of the borrower and spouse must be documented. Significant liabilities, to be deducted from the total income in determining ability to meet the mortgage payments are accounts that, generally, are of a relatively long-term; i.e., 6 months or over. Other accounts for terms of less than 6 months must, of course, be considered in determining ability to meet family expenses. Certainly any account with less than 6 months' duration which requires payments so large as to cause a severe impact on the family's resources for any period of time must be considered in the loan analysis. For example, monthly payments of $100 on an auto loan with a remaining balance of $500 would be included in those obligations to be deducted from the total income regardless of the fact that the account can be expected to pay out in 5 months. It is clear that the applicant will, in this case, continue to carry the burden of those $100 payments for the first, most critical, months of the home loan. Similarly, when the credit information shows open accounts of several years' duration which are clearly of a revolving or open-end type, the regular monthly payment for such accounts should be considered as a long-term obligation to be deducted from income.

(7) *Requirements for verifications*. If the credit investigation reveals debts or obligations of a material nature which were not divulged by the applicant, lenders must be certain to obtain clarification as to the status of such debts from the borrower. A proper analysis is obviously not possible unless there is total correlation between the obligations claimed by the borrower and those revealed by a credit report or deposit verification. Conversely, significant debts and obligations reported by the borrower must be rated. If the credit report fails to provide necessary information on such accounts, lenders will be expected to obtain their own verifications of those debts directly from the creditors. Credit reports and verifications must be no more than 90 days old to be considered valid. For loans closed automatically, this requirement will be considered satisfied if the date of the credit report or verification is within 90 days of the date of the veteran's application to the lender. Of major significance are the applicant's rental history and outstanding or recently retired mortgages, if any, and lenders should be sure ratings on such accounts are obtained. A determination is necessary as to whether alimony and/or child support payments are required. Verification of the amount of such obligations should be obtained although documentation concerning an applicant's divorce should not be obtained automatically unless it is necessary to verify the amount of any alimony or child support liability indicated by the applicant. If in the routine course of processing the loan application, however, direct evidence is received (e.g., from the credit report) that an obligation to pay alimony or child support exists (as opposed to mere evidence that the veteran was previously divorced), the discrepancy between the loan application and credit report can and should be fully resolved in the same manner as any other such discrepancy would be handled.

(8) *Job-related expenses*. Known job-related expenses should be documented. This will include costs for any dependent care, union dues, significant commuting costs, etc. When a family's circumstances are such that dependent care arrangements would probably be necessary, it is important to determine the cost of such services in order to arrive at an accurate total of deductions.

(9) *Credit reports*. Credit reports obtained by lenders on VA guaranteed loan applications must be in conformance with the Residential Mortgage Credit Report Standards formulated jointly by the Department of Veterans Affairs, Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Federal Housing

Administration, Farmers Home Administration, credit repositories, repository affiliated consumer reporting agencies and independent consumer reporting agencies. The Residential Mortgage Credit Report is a detailed account of the credit, employment, and residence history as well as public records information concerning an individual. From time to time the Secretary as well as the entities listed above will provide the names of the national organizations that provide credit reports meeting the requirements of the Residential Mortgage Credit Report Standards. The names of such organizations are available through VA and other participating entities. All credit reports obtained by the lender must be submitted to VA.

(f) *Borrower's personal and financial status*. The number and ages of dependents have an important bearing on whether income after deduction of fixed charges is sufficient to support the family. Type and duration of employment of both the borrower and spouse are important as an indication of stability of their employment. The amount of liquid assets owned by the borrower or spouse, or both, is an important factor in determining that they have sufficient funds to close the loan, as well as being significant in analyzing the overall qualifications for the loan. (It is imperative that adequate cash assets from the veteran's own resources are verified to allow the payment of any difference between the sales price of the property and the loan amount, in addition to that necessary to cover closing costs, if the sales price exceeds the reasonable value established by VA (38 CFR 36.4336(a)(3)). Verifications must be no more that 90 days old to be considered valid. For loans closed on the automatic basis, this requirement will be considered satisfied if the date of the deposit verification is within 90 days of the date of the veteran's application to the lender. Current monthly rental or other housing expense is an important consideration when compared to that to be undertaken in connection with the contemplated housing purchase.

(g) *Estimated monthly shelter expenses*. It is important that monthly expenses such as taxes, insurance, assessments and maintenance and utilities be estimated accurately based on property location and type of house; e.g., old or new, large or small, rather than using or applying a "rule of thumb" to all properties alike. Maintenance and utility amounts for various types of property should be realistically estimated. Local utility companies should be consulted for current rates. The age and type of construction of a house may well affect these expenses. In the case of condominiums or houses in a planned unit development (PUD), the monthly-amount of the maintenance assessment payable to a homeowners association should be added. If the amount currently assessed is less than the maximum provided in the covenants or master deed, and it appears likely that the amount will be insufficient for operation of the condominium or PUD, the amount used will be the maximum the veteran could be charged. If it is expected that real estate taxes will be raised, or if any special assessments are expected, the increased or additional amounts should be used. In special flood hazard areas, include the premium for any required flood insurance.

(h) *Lender responsibility*.

(1) Lenders are fully responsible for developing all credit information; i.e., for obtaining verifications of employment and deposit, credit reports, and for the accuracy of the information contained in the loan application.

(2) Verifications of employment and deposits, and requests for credit reports and/or credit information must be initiated and received by the lender.

(3) In cases where the real estate broker/agent, or any other party requests any of this information, the report(s) must be returned directly to the lender. This fact must be

disclosed by appropriately completing the required certification on the loan application or report and the parties must be identified as agents of the lender.

(4) Where the lender relies on other parties to secure any of the credit or employment information or otherwise accepts such information obtained by any other party such parties shall be construed for purposes of the submission of the loan documents to VA to be authorized agents of the lender, regardless of the actual relationship between such parties and the lender, even if disclosure is not provided to VA under paragraph (h)(3) of this section. Any negligent or willful misrepresentation by such parties shall be imputed to the lender as if the lender had processed those documents and the lender shall remain responsible for the quality and accuracy of the information provided to VA.

(5) All credit reports secured by the lender or other parties as identified in paragraphs (h)(3) and (h)(4) of this section shall be provided to VA. If updated credit reports reflect materially different information than that in other reports such discrepancies must be explained by the lender and the ultimate decision as to the effects of the discrepancy upon the loan application fully addressed by the underwriter.

(6) Lender originating loans are responsible for determining and certifying to VA on the appropriate application or closing form that the loan meets all statutory and regulatory requirements. Lenders will affirmatively certify that loans were made in full compliance with the law and loan guaranty regulations as prescribed in these regulations.

(i) *Definitions*.

(1) The definitions contained in part 42 of this chapter are applicable in this section.

(2) *Another Appropriate Amount*. In determining the appropriate amount of a lender's civil penalty in cases where the Secretary has not sustained a loss or where two times the amount of the Secretary's loss on the loan involved does not exceed $10,000, the Secretary shall consider:

(i) The materiality and importance of the false certification to the determination to issue the guaranty, or to approve the assumption;

(ii) The frequency and past pattern of such false certifications by the lender; and,

(iii) Any exculpatory or mitigating circumstances.

(3) *Complaint* includes the assessment of liability served pursuant to this subsection.

(4) *Defendant* means a lender named in the complaint.

(5) *Lender* includes the holder approving loan assumptions pursuant to 38 U.S.C. 3714.

(j) *Procedures for certification*.

(1) As a condition to VA issuance of a loan guaranty on all loans closed on or after the effective date of these regulations, and as a prerequisite to an effective loan assumption on all loans assumed pursuant to 38 U.S.C. 3714 on or after the effective date of these regulations, the following certification shall accompany each loan closing or assumption package:

"The undersigned lender certifies that the (loan) (assumption) application, all verifications of employment, deposit, and other income and credit verification documents have been processed in compliance with 38 CFR part 36; that all credit reports obtained or generated in connection with the processing of this borrower's (loan) (assumption) application have been provided to VA; that, to the best of the undersigned lender's knowledge and belief the (loan) (assumption) meets the underwriting standards recited in 38 U.S.C. chapter 37 and 38 CFR part 36; and that all information provided in support of this (loan) (assumption) is true, complete and accurate to the best of the undersigned lender's knowledge and belief."

(2) The certification shall be executed by an officer of the lender authorized to execute documents and act on behalf of the lender.

(3) Any lender who knowingly and willfully makes a false certification required pursuant to §36.3447(j)(1) shall be liable to the United State Government for a civil penalty equal to two times the amount of the Secretary's loss on the loan involved or to another appropriate amount, not to exceed $10,000, whichever is greater.

(k) *Assessment of liability*.

(1) Upon an assessment confirmed by the Chief Benefits Director, in consultation with the Investigating Official, that a certification, as required in this section, is false, a report of findings of the Chief Benefits Director shall be submitted to the Reviewing Official setting forth:

(i) The evidence that supports the allegations of a false certification and of liability;

(ii) A description of the claims or statements upon which the allegations of liability are based;

(iii) The amount of the VA demand to be made; and,

(iv) Any exculpatory or mitigating circumstances that may relate to the certification.

(2) The Reviewing Official shall review all of the information provided and will either inform the Chief Benefits Director and Investigating Official that there is not adequate evidence, that the lender is liable, or serve a complaint on the lender stating:

(i) The allegations of a false certification and of liability;

(ii)The amount being assessed by the Secretary and the basis for the amount assessed;

(iii) Instructions on how to satisfy the assessment and how to file an answer to request a hearing, including a specific statement of the lender's right to request a hearing by filing an answer and to be represented by counsel; and

(iv) That failure to file an answer within 30 days of the complaint will result in the imposition of the assessment without right to appeal the assessment to the Secretary.

(l) *Hearing procedures*. A lender hearing on an assessment established pursuant to this section shall be governed by the procedures recited at 38 CFR 42.8 through 42.47.

(m) *Additional remedies*. Any assessment under this section may be in addition to other remedies available to VA, such as debarment and suspension pursuant to 38 U.S.C. 3704 and part 44 of this chapter or loss of automatic processing authority pursuant to 38 U.S.C. 3702, or other actions by the Government under any other law including but not limited to title 18, U.S.C. and 31 U.S.C 3732. (Authority: 38 U.S.C. 3710).

§36.4338 DEATH OR INSOLVENCY OF HOLDER

(a) Immediately upon the death of the holder and without the necessity of request or other action by the debtor or the Secretary, all sums then standing as a credit balance in a trust, or deposit, or other account to cover taxes, insurance accruals, or other items in connection with the loan secured by the encumbered property, whether stated to be such or otherwise designated, and which have not been credited on the note shall, nevertheless, be treated as a setoff and shall be deemed to have been credited thereon as of the date of the last debit to such account, so that the unpaid balance of the note as of that date will be reduced by the amount of such credit balance:

Provided, That any unpaid taxes, insurance premiums, ground rents, or advances may be paid by the holder of the indebtedness, at the holder's option, and the amount which otherwise would have been deemed to have been credited on the note reduced accordingly. This paragraph shall be applicable whether the estate of the deceased holder is solvent or insolvent.

(b) The provisions of paragraph (a) of this section shall also be applicable in the event of:

(1) Insolvency of holder;

(2) Initiation of any bankruptcy or reorganization, or liquidation proceedings as to the holder, whether voluntary or involuntary;

(3) Appointment of a general or ancillary receiver for the holder's property; or in any case

(4) Upon the written request of the debtor if all secured and due insurance premiums, taxes, and ground rents have been paid, and appropriate provisions made for future accruals.

(c) Upon the occurrence of any of the events enumerated in paragraph (a) or (b) of this section, interest on the note and on the credit balance of the deposits mentioned in paragraph (a) shall be set off against each other at the rate payable on the principal of the note, as of the date of last debit to the deposit account. Any excess credit of interest shall be treated as a set-off against the unpaid advances, if any and the unpaid balance of the note.

(d) The provisions of paragraphs (a), (b) and (c) of this section shall apply also to corporations. The dissolution thereof by expiration of charter, by forfeiture, or otherwise shall be treated as is the death of an individual as provided in paragraph (a) of this section.

§36.4339 QUALIFICATION FOR DESIGNATED FEE APPRAISERS

To qualify for approval as a designated fee appraiser, an applicant must show to the satisfaction of the Secretary that his or her character, experience, and the type of work in which he or she has had experience for at least 5 years qualifies the applicant to competently appraise and value within a prescribed area the type of property to which the approval relates.

§36.4340 RESTRICTION ON DESIGNATED FEE APPRAISERS

(a) A designated fee appraiser shall not make an appraisal, excepting of alterations, improvements, or repairs to real property entailing a cost of not more than $3,500, if such appraiser is an officer, director, trustee, employer, or employee of the lender, contractor, or vendor.

(b) An appraisal made by a designated fee appraiser shall be subject to review and adjustment by the Secretary. The amount determined to be proper upon any such review or adjustment shall constitute the "reasonable value" for the purpose of determining the eligibility of the related loan.

§36.4342 DELEGATION OF AUTHORITY

(a) Except as hereinafter provided, each employee of the Department of Veterans Affairs heretofore or hereafter appointed to, or lawfully filling, any position designated in paragraph (b) of this section is hereby delegated authority, within the limitations and conditions prescribed by law, to exercise the powers and functions of the Secretary with respect to the guaranty or insurance of loans and the rights and liabilities arising therefrom, including but not limited to the adjudication and allowance, disallowance, and compromise of claims; the collection or compromise of amounts due, in money or other property; the extension, rearrangement, or acquisition of loans; the management and disposition of secured and unsecured notes and other property; and those functions expressly or impliedly embraced within paragraphs (2) to (6), inclusive, of 38 U.S.C. 3720(a). Incidental to the exercise and performance of the powers and functions hereby delegated, each such employee is authorized to execute and deliver (with or without acknowledgment) for, and on behalf of, the Secretary, evidence of guaranty or of insurance credits and such certificates, forms, conveyances, and other instruments as may be appropriate in connection with the acquisition, ownership, management, sale, transfer, assignment, encumbrance, rental, or other disposition of real or personal property or of any right, title, or interest therein, including, but not limited to, contracts of sale, installment contracts, deeds, leases, bills of sale, assignments, and releases; and to approve disbursements to be made for any purpose authorized by 38 U.S.C., chapter 37.

(b) Designated positions:

Chief Benefits Director
Director, Loan Guaranty Service
Director, Medical and Regional Office Center
Director, Regional Office and Insurance Center
Director, VA Regional Office
Loan Guaranty Officer
Assistant Loan Guaranty Officer

The authority hereby delegated to employees of the positions designated in this paragraph may, with the approval of the Chief Benefits Director, be redelegated.

(c) Nothing in this section shall be construed (1) to authorize any such employee to exercise the authority vested in the Secretary under 38 U.S.C. 501(a) or 3703(a)(2) or to sue, or enter appearance for and on behalf of the Secretary, or confess judgment against the Secretary in any court without the Secretary's prior authorization; or (2) to include the authority to exercise those powers delegated to the Chief Benefits Director, or the Director, Loan Guaranty Service, under §36.4320(j), 36.4335, or 36.4343:

Provided, That, anything in the regulations concerning guaranty or insurance of loans to veterans to the contrary notwithstanding, any evidence of guaranty or insurance issued on or after July 1, 1948, by any of the employees designated in paragraph (b) of this section or by any employee designated an authorized agent or a loan guaranty agent shall be deemed to have been issued by the Secretary, subject to the defenses reserved in 38 U.S.C. 3721.

(d) Each Regional Office, regional office and insurance center, and Medical and Regional Office Center shall maintain and keep current a cumulative list of all employees of that Office or Center who, since May 1, 1980, have occupied the positions of Director, Loan Guaranty Officer, and Assistant Loan Guaranty Officer. This list will include each employee's name, title, date the employee assumed the position, and the termination date, if applicable, of the employee's tenure in such position. The list shall be available for public inspection and copying at the Regional Office, or Center, during normal business hours. (Authority: 38 U.S.C. 501(a)(1), 3720(a)(5))

§36.4343 COOPERATIVE LOANS

(a) Any loan, which is (1) related to an enterprise in which more than 10 individuals will participate; or (2) to be made for the purchase or construction of residential units in any housing development, cooperative or otherwise, the title to which development or to the individual units therein is not to be held directly by the veteran-participants, or which contemplates the ownership or maintenance of more than three units or of their major appurtenances in common, to be eligible for guaranty or insurance shall require prior approval of the Chief Benefits Director, or the Director, Loan Guaranty Service, who may issue such approval upon such conditions and limitations deemed appropriate, not inconsistent with the provisions of 38 U.S.C., chapter 37 and regulations concerning guaranty or insurance of loans to veterans.

(b) The issuance of such approval with respect to residential development under paragraph (a)(2) of this section also shall be subject to such conditions and stipulation as in the judgment of the approving officer are possible and proper to (1) afford reasonable and feasible protection to the rights of the Government as guarantor or insurer, and as subrogee, and to each veteran-participant against loss of his or her respective equity consequent upon the failure of other participants to discharge their obligations; (2) provide for a reasonable and workable plan for the operation and management of the project; (3) limit the personal liability of each veteran-participant to those sums allocable on a proper ratable basis to the purchase, cost, and maintenance of his or her individual unit or participating interest; (4) limit commercial features to those reasonably calculated to promote the economic soundness of the project and the living convenience of the participants, retaining the essential character of a residential project.

(c) No such project, development, or enterprise may be approved which involves an initial grouping of more then 500 veterans, or a cost of more than five million dollars, unless it is conclusively shown to the satisfaction of the approving officer that a greater number of veterans or dollar amount will assure substantial advantages to the veteran-participants which could not be achieved in a smaller project.

(d) When approved as in this section provided, and upon performance of the conditions indicated in the prior approval, proper guaranty certificate or certificates may be issued in connection with the loan or loans to be guaranteed on behalf of eligible veterans participating in the project, development or enterprise not to exceed in total amount the sum of the guaranties applied for by the individual participants and for which guaranty each participant is then eligible.

(e) In lieu of guaranty as authorized in paragraph (d) of this section, insurance shall be available on application by the lender and all veterans concerned. In such case the insurance credit shall be limited to 15 percent of the obligation of the veteran-applicant (subject to available eligibility) and the total insurance credit in respect to the veterans' loans involved in the project shall not exceed 15 percent of the aggregate of the principal sums of the individual indebtedness incurred by the veterans participating in the project for the purpose of acquiring their respective interests therein.

§36.4344 LENDER APPRAISAL PROCESSING PROGRAM

(a) *Delegation of Authority to Lenders to Review Appraisals and Determine Reasonable Value*

(1) To be eligible for delegation of authority to review VA appraisals and determine the reasonable value of properties to be purchased with VA guaranteed loans, a lender must (i) have automatic processing authority under 38 U.S.C. 3702(d), and (ii) employ one or more staff appraisal reviewers acceptable to the Secretary.

(2) To qualify as a lender's staff appraisal reviewer an applicant must be a full-time member of the lender's permanent staff and may not be employed by, or perform services for, any other mortgagee. The individual must not engage in any private pursuits in which there will be, or appear to be, any conflict of interest between those pursuits and his/her duties, responsibilities, and performance as a Lender Appraisal Processing Program (LAPP) staff appraisal reviewer. Three years of experience is necessary to qualify as a lender's staff appraisal reviewer. That experience must demonstrate a knowledge of, and the ability to apply industry-accepted principles, methods, practices and techniques of appraising, and the ability to competently determine the value of property within a prescribed geographical area. The individual must demonstrate the ability to review the work of others and to recognize deviations from accepted appraisal principles, practices, and techniques, errors in computations, and unjustifiable and unsupportable conclusions.

(3) Lenders that meet the requirements of 38 U.S.C. 3702(d), and have a staff appraisal reviewer determined acceptable by VA, will be authorized to review appraisals and make reasonable value determinations on properties that will be security for VA guaranteed loans. The lender's authorization will be subject to a one-year probationary period. Additionally, lenders must satisfy initial and subsequent VA office case review requirements prior to being allowed to determine reasonable value without VA involvement. The initial office case review requirement must be satisfied in the VA regional office in whose jurisdiction the lender's staff appraisal reviewer is located before the LAPP authority may be utilized by that lender in any other VA office's jurisdiction.

To satisfy the initial office case review requirement, the first five cases of each lender staff appraisal reviewer involving properties in the regional office location where the staff appraisal reviewer is located will be processed by him or her up to the point where he or she has made a reasonable value determination and fully drafted, but not issued, the lender's notification of reasonable value letter to the veteran. At that point, and prior to loan closing, each of the five cases will be submitted to the local VA office. After a staff review of each case, VA will issue a Certificate of Reasonable Value, which the lender may use in closing the loan automatically if it meets all other requirements of the VA. If these five cases are found to be acceptable by VA, the lender's staff appraisal reviewer will be allowed to fully process subsequent appraisals for properties located in that VA office's jurisdiction without prior submission to VA and issuance by VA of a Certificate of Reasonable Value. Lenders must also satisfy a subsequent VA office case review requirement in each additional VA office location in which they desire to extend and utilize this authority. Under this requirement, the lender must have first satisfied the initial office case review requirement and then must submit to the additional VA office(s) the first case each staff appraisal reviewer processes in the jurisdiction of that office. As provided under the initial office case review requirement, VA office personnel will issue a Certificate of Reasonable value for this case and subsequently determine the acceptability of the lender's staff appraisal reviewer's processing. If VA finds this first case to be acceptable, the lender's staff appraisal reviewer will be allowed to fully process subsequent cases in that additional VA office's jurisdiction without prior submission to VA. The initial and subsequent office case review requirements may be expanded by VA if acceptable performance has not been demonstrated. After satisfaction of the initial and subsequent office case review requirements, routine reviews of LAPP cases will be made by VA staff based upon quality control procedures established by the Chief Benefits Director. Such review will be made on a random sampling or performance related basis. During the probationary period a high percentage of reviews will be made by VA staff.

(4) The following certification by the lender's nominated staff appraisal reviewer must be provided with the lender's application for delegation of LAPP authority:

> I hereby acknowledge and represent that by signing the Uniform Residential Appraisal Report (URAR), FHLMC (Federal Home Loan Mortgage Corporation) Form 70/FNMA (Federal Notice Mortgage Association) Form 1004, I am certifying, in all cases, that I have personally reviewed the appraisal report. In doing so I have considered and utilized recognized professional appraisal techniques, have found the appraisal report to have been prepared in compliance with applicable VA requirements, and concur with the recommendations of the fee appraiser, who was assigned by VA to the case. Furthermore, in those cases where clarifications or corrections have been requested from the VA fee appraiser there has been no pressure or influence exerted on that appraiser to remove or change information that might be considered detrimental to the subject property, or VA's interests, or to reach a predetermined value for that property.
>
> Signature of Staff Appraisal Reviewer.

(5) Other certifications required from the lender will be specified with particularity in the separate instructions issued by the Secretary, as noted in §36.4344(b).

(b) *Instructions for LAPP Procedures*. The Secretary will publish separate instructions for processing appraisals under the Lenders Appraisal Processing Program. Compliance with these regulations and the separate instructions issued by the Secretary is deemed by VA to be the minimum exercise of due diligence in processing LAPP cases. Due diligence is considered by VA to represent that care, as is to be properly expected

from, and ordinarily exercised by, reasonable and prudent lenders who would be dependent on the property as security to protect its investment.

(c) *VA Minimum Property Requirements*. Lenders are responsible for determining that the property meets VA minimum property requirements. The separate instructions issued by the Secretary will set forth the lender's ability to adjust, remove, or alter the fee appraiser's or fee compliance inspector's recommendations concerning VA minimum property requirements. Condominiums, planned-unit developments and leasehold estates must have been determined acceptable by VA. A condominium or planned-unit development which is acceptable to the Department of Housing and Urban Development or the Department of Agriculture may also be acceptable to VA.

(d) *Adjustment of Value Recommendations*. The amount of authority to upwardly adjust the fee appraiser's estimated market value during the lender staff appraisal reviewer's initial review of the appraisal report or to subsequently process an appeal of the lender's established reasonable value will be specified in the separate instructions issued by VA as noted in §36.4344(b). The amount specified must not in any way be considered an administrative adjustment figure which may be applied indiscriminately and without valid basis or justification with the sole purpose of reaching an amount necessary to complete the sale or mortgage transaction.

(1) *Adjustment During Initial Review*. Any adjustment during the staff appraisal reviewer's initial review of the appraisal report must be fully and clearly justified in writing on the appraisal report form or, if necessary, on an addendum. The basis for the adjustment must be adequate and reasonable by professional appraisal standards. If real estate market or other valid data was utilized in arriving at the decision to make the adjustment, such data must be attached to the appraisal report. All adjustments, comments, corrections, justifications, etc., to the appraisal report must be made in a contrasting color, be clearly legible, and signed and dated by the staff appraisal reviewer.

(2) *Processing Appeals*. The authority provided under 38 U.S.C. 3731(d) which permits a lender to obtain a VA fee panel appraiser's report which VA is obligated to consider in an appeal of the established reasonable value shall not apply to cases processed under the authority provided by this section. All appeals of VA fee appraisers' estimated market values or lenders' reasonable value determinations above the amount specified in the separate instructions issued by VA must be submitted, along with the lender's recommendations, if any, to VA for processing and final determination. Unless otherwise authorized in the separate instructions lenders must also submit appeals, regardless of the amount, to VA in all cases where the staff appraisal reviewer has made an adjustment during their initial review of the appraisal report to the fee appraiser's market value estimate. The fee appraiser's estimated market value or lender's reasonable value determination may be increased only when such increase is clearly warranted and fully supported by real estate market or other valid data considered adequate and reasonable by professional appraisal standards and the lender's staff appraisal reviewer clearly and fully justifies the reasoning and basis for the increase in writing on the appraisal report form or an addendum. The staff appraisal reviewer must date and sign the written justification and must cite within it the data used in arriving at the decision to make the increase. All such data shall be attached to the appraisal report form and any addendum.

(e) *Notification*. It will be the responsibility of the lender to notify the veteran borrower in writing of the determination of reasonable value and related conditions specific to the property and to provide the veteran with a copy of the appraisal report. Any delay in processing the notification of value must be documented. Any delay of

more than five work days between the date of the lender's receipt of the fee appraiser's report and date of the notification of value to the veteran, without reasonable and documented extenuating circumstances, will not be acceptable. A copy of the lender notification letter to the veteran and the appraisal report must be forwarded to the VA office of jurisdiction at the same time the veteran is notified. In addition, the original appraisal report, related appraisal documentation, and a copy of the reasonable value determination notification to the veteran must be submitted to the VA with the request for loan guaranty.

(f) *Indemnification*. When the Secretary has incurred a loss as a result of a payment of claim under guaranty and in which the Secretary determines an increase made by the lender under §36.4344(d) or (f) was unwarranted, or arbitrary and capricious, the lender shall indemnify the Secretary to the extent the Secretary determines such loss was caused, or increased, by the increase in value.

(g) *Affiliations*. A lender affiliated with a real estate firm builder, land developer or escrow agent as a subsidiary division, investment or any other entity in which it has a financial interest or which it owns may not use this authority for any cases involving the affiliate unless the lender demonstrates to the Secretary's satisfaction that the lender and its affiliate(s) are essentially separate entities that operate independently of each other, free of all cross-influences (e.g., a formal corporate agreement exists which specifically sets forth this fact).

(h) *Quality Control Plans*. The lender must have an effective self-policing or quality control system to ensure the adequacy and quality of their LAPP staff appraisal reviewer's processing and, that its activities do not deviate from high standards of integrity. The quality control system must include frequent, periodic audits that specifically address the appraisal review activity. These audits may be performed by an independent party, or by the lender's independent internal audit division which reports directly to the firm's chief executive officer. The lender must agree to furnish findings and information under this system to VA on demand. While the quality control personnel need not be appraisers, they should have basic familiarity with appraisal theory and techniques and the ability to prescribe appropriate corrective action(s) in the appraisal review process when discrepancies or problems are identified. The basic elements of the system will be described in separate instructions issued by the Secretary. Copies of the lender's quality control plan or self-policing system evidencing appraisal related matters must be provided to the VA office of jurisdiction with the lender's application for LAPP authority.

(i) *Fees*. The Secretary may require mortgagees to pay an application fee and/or annual fees, including additional fees for each branch office authorized to process cases under the authority delegated under this section, in such amounts and at such times as the Secretary may require.

(j) *Withdrawal of Lender Authority*. The authority for a lender to determine reasonable value may be withdrawn by the Loan Guaranty Officer when proper cause exists. A lender's authority to make reasonable value determinations shall be withdrawn when the lender no longer meets the basic requirements for delegating the authority, or when it can be shown that the lender's reasonable value determinations have not been made in accordance with VA regulations, requirements, guidelines, instructions or applicable laws, or when there is adequate evidence to support reasonable belief by VA that a particular unacceptable act, practice, or performance by the lender or the lender's staff has occurred. Such acts, practices or performance include, but are not limited to: Demonstrated technical incompetence (i.e., conduct which demonstrates an insufficient

knowledge of industry accepted appraisal principles, techniques and practices; or the lack of technical competence to review appraisal reports and make value determinations in accordance with those requirements); substantive or repetitive errors (i.e., any error(s) of a nature that would materially or significantly affect the determination of reasonable value or condition of the property; or a number or series of errors that, considered individually, may not significantly impact the determination of reasonable value or property condition, but which when considered in the aggregate would establish that appraisal reviews or LAPP case processing are being performed in a careless or negligent manner), or continued instances of disregard for VA requirements after they have been called to the lender's attention.

(1) Withdrawal of authority by the Loan Guaranty Officer may be either for an indefinite or a specified period of time. For any withdrawal longer than 90 days a reapplication for lender authority to process appraisals under these regulations will be required. Written notice will be provided at least 30 days in advance of withdrawal unless the Government's interests are exposed to immediate risk from the lender's activities in which case the withdrawal will be effected immediately. The notice will clearly and specifically set forth the basis and grounds for the action. There is no right to a formal hearing to contest the withdrawal of LAPP processing privileges. However, if within 15 days after receiving notice the lender requests an opportunity to contest the withdrawal, the lender may submit, in person, in writing, or through a representative, information and argument to the Loan Guaranty Officer in opposition to the withdrawal. The Loan Guaranty Officer will make a recommendation to the Regional Office Director who shall make the determination as to whether the action should be sustained, modified or rescinded. The lender will be informed in writing of the decision.

(2) The lender has the right to appeal the Regional Office Director's decision to the Chief Benefits Director. In the event of such an appeal, the Chief Benefits Director will review all relevant material concerning the matter and make a determination that shall constitute final agency action. If the lender's submission in opposition raises a genuine dispute over facts material to the withdrawal of LAPP authority, the lender will be afforded an opportunity to appear with a representative, submit documentary evidence, present witnesses and confront any witness the Veterans Benefits Administration presents. The Chief Benefits Director will appoint a hearing officer or panel to conduct the hearing. When such additional proceedings are necessary, the Chief Benefits Director shall base the determination on the facts as found, together with any information and argument submitted by the lender.

(3) In actions based upon a conviction or civil judgment, or in which there is no genuine dispute over material facts, the Chief Benefits Director shall make a decision on the basis of all the information in the administrative record, including any submission made by the lender.

(4) Withdrawal of the LAPP authority will require that VA make subsequent determinations of reasonable value for the lender. Consequently, VA staff will review each appraisal report and issue a Certificate of Reasonable Value which can then be used by the lender to close loans on either the prior VA approval or automatic basis.

(5) Withdrawal by VA of the lender's LAPP authority does not prevent VA from also withdrawing automatic processing authority or taking debarment or suspension action based upon the same conduct by the lender. (Authority: 38 U.S.C. 3731)

§36.4345 WAIVERS, CONSENTS, AND APPROVALS; WHEN EFFECTIVE

No waiver, consent, or approval required or authorized by the regulations concerning guaranty or insurance of loans to veterans shall be valid unless in writing signed by the Secretary or the subordinate officer to whom authority has been delegated by the Secretary.

§36.4346 SERVICING PROCEDURES FOR HOLDERS

(a) *Establishment of loan servicing program*. The holder of a loan guaranteed or insured by the Secretary shall develop and maintain a loan servicing program which follows accepted industry standards for servicing of similar type conventional loans. The loan servicing program established pursuant to this section may employ different servicing approaches to fit individual borrower circumstances and avoid establishing a fixed routine. However, it must incorporate each of the provisions specified in paragraphs (b) through (1) of this section.

(b) *Procedures for providing information*.

(1) Loan holders shall establish procedures to provide loan information to borrowers, arrange for individual loan consultations upon request and maintain controls to assure prompt responses to inquiries. One or more of the following means of making information readily available to borrowers is required.

(i) An office staffed with trained servicing personnel with access to loan account information located within 200 miles of the property.

(ii) Toll-free telephone service or acceptance of collect telephone calls at an office capable of providing needed information.

(2) All borrowers must be informed of the system available for obtaining answers to loan inquiries, the office from which the needed information may be obtained, and reminded of the system at least annually.

(c) *Statement for income tax purposes*. Within 60 days after the end of each calendar year, the holder shall furnish to the borrower a statement of the interest paid and, if applicable, a statement of the taxes disbursed from the escrow account during the preceding year. At the borrower's request, the holder shall furnish a statement of the escrow account sufficient to enable the borrower to reconcile the account.

(d) *Change of servicing*. Whenever servicing of a loan guaranteed or insured by the Secretary is transferred from one holder to another, notice of such transfer by both the transferor and transferee, the form and content of such notice, the timing of such notice, the treatment of payments during the period of such transfer, and damages and costs for failure to comply with these requirements shall be governed by the pertinent provisions of the Real Estate Settlement Procedures Act as administered by the Department of Housing and Urban Development.

(e) *Escrow accounts*. A holder of a loan guaranteed or insured by the Secretary may collect periodic deposits from the borrower for taxes and/or insurance on the security and maintain a tax and insurance escrow account provided such a requirement is authorized under the terms of the security instruments. In maintaining such accounts, the holder shall comply with the pertinent provisions of the Real Estate Settlement Procedures Act.

(f) *System for servicing delinquent loans*. In addition to the requirements of the Real Estate Settlement Procedures Act, concerning the duties of the loan servicer to respond to borrower
inquiries, to protect the borrower's credit rating during a payment dispute period, and to pay damages and costs for noncompliance, holders shall establish a system for servicing delinquent loans which ensures that prompt action is taken to collect amounts due from borrowers and minimize the number of loans in a default status. The holder's servicing system must include the following:

(1) An accounting system which promptly alerts servicing personnel when a loan becomes delinquent;

(2) A collection staff which is trained in techniques of loan servicing and counseling delinquent borrowers to advise borrowers how to cure delinquencies, protect their equity and credit rating and, if the default is insoluble, pursue alternatives to foreclosure;

(3) Procedural guidelines for individual analysis of each delinquency;

(4) Instructions and appropriate controls for sending delinquent notices, assessing late charges, handling partial payments, maintaining servicing histories and evaluating repayment proposals;

(5) Management review procedures for evaluating efforts made to collect the delinquency and the response from the borrower before a decision is made to initiate action to liquidate a loan;

(6) Procedures for reporting delinquencies of 90 days or more and loan terminations to major consumer credit bureaus as specified by the Secretary and for informing borrowers that such action will be taken; and

(7) Controls to ensure that all notices required to be given to the Secretary on delinquent loans are provided timely and in such form as the Secretary shall require.

(g) *Collection actions*.

(1) Holders shall employ collection techniques which provide flexibility to adapt to the individual needs and circumstances of each borrower. A variety of collection techniques may be used based on the holder's determination of the most effective means of contact with borrowers during various stagesm of delinquency. However, at a minimum the holder's collection procedures must include the following actions:

(i) A written delinquency notice to the borrower(s) requesting immediate payment if a loan installment has not been received within 17 days after the due date. This notice must be mailed no later than the 20th day of the delinquency and state the amount of the payment and of any late charges that are due.

(ii) An effort, concurrent with the written delinquency notice to establish contact with the borrower(s) by telephone. When talking with the borrower(s), the holder should attempt to determine why payment was not made and emphasize the importance of remitting loan installments as they come due.

(iii) A letter to the borrower(s) if payment has not been received within 30 days after it is due and telephone contact could not be made. This letter should emphasize the seriousness of the delinquency and the importance of taking prompt action to resolve the

default. It should also notify the borrower(s) that the loan is in default, state the total amount due and advise the borrower(s) how to contact the holder to make arrangements for curing the default.

(iv) In the event the holder has not established contact with the borrower(s) and has not determined the financial circumstances of the borrower(s) or established a reason for the default or obtained agreement to a repayment plan from the borrower(s), then a face-to-face interview with the borrower(s) or a reasonable effort to arrange such a meeting is required.

(2) The holder must provide a valid explanation of any failure to perform these collection actions when reporting loan defaults to the Secretary. A pattern of such failure may be a basis for sanctions under 38 CFR §36.4331.

(h) *Conducting interviews with delinquent borrowers*. When personal contact with the borrower(s) is established, the holder shall solicit sufficient information to properly evaluate the prospects for curing the default and whether the granting of forbearance or other relief assistance would be appropriate. At a minimum, the holder must make a reasonable effort to establish the following:

(1) The reason for the default and whether the reason is a temporary or permanent condition;

(2) The present income and employment of the borrower(s);

(3) The current monthly expenses of the borrower(s) including household and debt obligations;

(4) The current mailing address and telephone number of the borrower(s); and

(5) A realistic and mutually satisfactory arrangement for curing the default.

(i) *Property inspections*.

(1) The holder shall make an inspection of the property securing the loan whenever it becomes aware that the physical condition of the security may be in jeopardy. Unless a repayment agreement is in effect, a property inspection shall also be made at the following times:

(i) Before the 60th day of delinquency or before initiating action to liquidate a loan, whichever is earlier; and,

(ii) At least once each month after liquidation proceedings have been started unless servicing information shows the property remains owner-occupied.

(2) Whenever a holder obtains information which indicates that the property securing the loan is abandoned, it shall make appropriate arrangements to protect the property from vandalism and the elements. Thereafter, the holder shall schedule inspections at least monthly to prevent unnecessary deterioration due to vandalism, or neglect. With respect to any loan more than 30 days delinquent, a property abandonment must be reported to the Secretary and appropriate action initiated under _ §36.4317(a) within 15 days after the holder confirms the property is abandoned.

(j) *Collection records*. The holder shall maintain individual file records of collection action on delinquent loans and make such records available to the Secretary for inspection on request. Such collection records shall show:

(1) The dates and content of letters and notices which were mailed to the borrower(s);

(2) Dated summaries of each personal servicing contact and the result of same;

(3) The indicated reason(s) for default; and,

(4) The date and result of each property inspection.

(k) *Reporting to the Secretary*. A summary of collection efforts, the information obtained through such efforts and the holder's evaluation of the reason for the default and prospects for resolution of the default must be included in any notice provided to the Secretary pursuant to __ §36.4315 and §36.4317.

(l) *Quality control procedures*. No later than 180 days after the effective date of this regulation, each loan holder shall establish internal controls to periodically assess the quality of the servicing performed on loans guaranteed by the Secretary and assure that all requirements of this section are being met. Those procedures must provide for a review of the holder's servicing activities at least annually and include an evaluation of delinquency and foreclosure rates on loans in its portfolio which are guaranteed by the Secretary. As part of its evaluation of delinquency and foreclosure rates, the holder shall:

(1) Collect and maintain appropriate data on delinquency and foreclosure rates to enable the holder to evaluate effectiveness of its collection efforts;

(2) Determine how its VA delinquency and foreclosure rates compare with rates in reports published by the industry, investors and others; and,

(3) Analyze significant variances between its foreclosure and delinquency rates and those found in available reports and publications and take appropriate corrective action.

(m) Holders shall provide available statistical data on delinquency and foreclosure rates and their analysis of such data to the Secretary upon request.

§36.4347 MINIMUM PROPERTY AND CONSTRUCTION REQUIREMENTS

No loan for the purchase or construction of residential property shall be eligible for guaranty or insurance unless such property complies or conforms with those standards of planning, construction, and general acceptability that may be applicable thereto and prescribed by the Secretary pursuant to 38 U.S.C. 3704(a).

§36.4348 AUTHORITY TO CLOSE LOANS ON THE AUTOMATIC BASIS

(a) Supervised lenders of the classes described in 38 U.S.C. 3702(d)(1) and (2) are authorized by statue to process VA guaranteed home loans on the automatic basis. This category of lenders includes any Federal land bank, national bank, State bank, private bank, building and loan association, insurance company, credit union or mortgage and loan company that is subject to examination and supervision by an agency of the United States or of any State or by any State.

(b) Nonsupervised lenders of the class described in 38 U.S.C. 3702 (d)(3) must apply to the Secretary for authority to process loans on the automatic basis. The following minimum requirements must be met:

(1) *Minimum assets*. A minimum of $50,000 of working capital must be maintained. Working capital is defined as the excess of current assets over current liabilities. Current assets are defined as cash or other assets that could readily be converted into cash within 1 year on the normal accounting or business cycle. Current liabilities are defined as obligations that would be paid within a year on a normal accounting or business cycle. The lender's latest financial statements (profit and loss statements and balance sheets), audited and certified by a CPA (certified public accountant), must accompany the application. If the date of the financial statement precedes that of the application by more than 6 months, the lender-applicant must also attach a copy of its latest internal quarterly report. In addition, the lender-applicant must agree that if the application is approved, the applicant will provide within 120 days following the end of its fiscal year an audited financial statement to the Director, Loan Guaranty Service for review.

(2) *Experience*. The firm must have been actively engaged in originating VA mortgages for at least three recent years. Alternately, each principal officer of the firm who is actively involved in managing origination functions must have a minimum of three recent years' total experience in the field of VA mortgages in managerial functions in either the present company of employment or in companies other than that of his or her present employment. In either case, every principal officer (president and vice presidents) must submit a resume of his or her experience in the mortgage lending field. Should the secretary and/or treasurer participate in the management of origination functions, they too must submit a resume and meet the minimum experience requirement if the company does not meet the experience requirement. Should the lender or any of its directors or officers ever have been debarred or suspended by any Federal agency or department or any of its directors or officers have been a director or officer of any other lender or corporation that was so debarred or suspended, or if the lender-applicant ever had a servicing contract with an investor terminated for cause, a statement of the facts must also be submitted.

(3) *Underwriter*. The senior officer of the firm must nominate and recommend a full-time qualified employee(s) to act in the firms behalf as underwriter(s) to personally review and make underwriting decisions associated with the submission of loans to VA which will be closed on the automatic basis. Nominees for underwriter must have a minimum of three years' experience in mortgage lending credit and making underwriting decisions, with at least two recent years in connection with loans submitted to VA for guaranty. This experience must have been with an institutional investor originating for its own portfolio or purchasing this type of loan, or with an originator selling this type of loan to investors.

(4) *Lines of credit*. The lender-applicant must have one or more lines of credit aggregating at least $1 million. The identity of the source(s) of warehouse lines of credit must be revealed to VA and the applicant must agree that VA may contact the named source(s) for the purpose of verifying the information.

(5) *Secondary market*. If the lender-applicant customarily sells loans it originates, it must have a minimum of two permanent investors. These may consist of the Government National Mortgage Association (GNMA) and other government agencies, including State housing agencies, and the Federal National Mortgage Association (FNMA).

(6) *Lender processing*. The lender-applicant must agree that all prospective VA loans will be reviewed at its home or main office prior to closing and the decision to make or reject the loan will be made at that office by an approved underwriter, unless VA authorizes that company to operate through regional underwriting offices.

(7) *Liaison*. The lender-applicant must designate one employee and an alternate to act as liaison on its behalf with VA. If possible, the lender-applicant should select employees other than VA approved underwriters to act as liaison with VA.

(8) *Courtesy closing*. The lender-applicant must certify to VA that it will not close loans on an automatic basis as a courtesy or accommodation for other mortgage lenders, whether or not such lenders are themselves approved to close on an automatic basis, without the express approval of VA. However, a lender with automatic authority may close loans for which information and supporting credit data have been developed on its behalf by a duly authorized agent.

(9) *Lender agents*. A lender using an agent or any other entity, such as a real estate broker, to perform a portion of the work involved in originating and closing a VA guaranteed loan on an automatic basis must take full responsibility by certification, on the appropriate VA form, or by corporate resolution for all acts, errors and omissions of the agent or other entity and its employees for the work performed. Any such acts, errors or omissions will be treated as those of the lender and appropriate sanctions may be imposed against the lender and its agent or any other entity developing information used by the lender in underwriting and processing the loan.

(10) *Subsidiaries/affiliates*. A lender approved for automatic processing may not close loans on the automatic basis for any builder, real estate broker, or other entity in which it has a financial interest or which it owns, is owned by, or with which it is affiliated. However, when the only relationship that exists between a lender and a builder is a construction loan, the lender may close the permanent mortgage on an automatic basis. This restriction may be eliminated for lenders that can provide documentation which demonstrates to VA's satisfaction that (i) the lender and builder or other affiliate are separate entities that operate independently of each other, and (ii) the percentage of all VA loans based on the affiliate's production originated by the lender during at least a one-year period on which payments are past due 90 days or more, is no higher that the national average for the same period for all mortgage loans.

(11) *Minimum use of automatic authority*. If approved, lenders should use their automatic authority to the maximum extent possible. Any lender with automatic authority who submits a loan on the prior approval basis will be required to submit an explanation from the VA approved underwriter as to why the loan was not closed automatically. Such a statement will not be needed for loans that must be processed on the prior approval basis; e.g., joint loans.

(12) *Probation*. Lender-applicants meeting the requirements of this section will be approved to close loans on an automatic basis for a one-year probationary period. Poor underwriting and/or consistently careless processing by the lender during the probationary period will be a basis for withdrawal of automatic authority.

(13) *Quality control system*. In order to be approved as a nonsupervised lender for automatic processing authority, the lender must implement a written quality control system which ensures compliance with VA requirements. The lender must agree to furnish findings under its systems to VA on demand. The elements of the quality control system must include the following:

(i) *Underwriting policies*. Each office of the mortgagee shall maintain copies of VA credit standards and all available VA underwriting guidelines.

(ii) *Corrective measures*. The system should ensure that effective corrective measures are taken promptly when deficiencies in loan originations are identified by either the lender or VA. Any cases involving major discrepancies which are discovered under the system must be reported to VA.

(iii) *System integrity*. The quality control system should be independent of the mortgage loan production function.

(iv) *Scope*. The review of underwriting decisions and certifications must include compliance with VA underwriting requirements, sufficiency of documentation and soundness of underwriting judgments.

(v) *Appraisal quality*. For lenders approved for the Lender Appraisal Processing Program (LAPP), the quality control system must specifically contain provisions concerning the adequacy and quality of real property appraisals. While the lender's quality control personnel need not be appraisers, they should have basic familiarity with appraisal theory and techniques so that they can select appropriate cases for review if discretionary sampling is used, and prescribe appropriate corrective action(s) in the appraisal review process when discrepancies or problems are identified. Copies of the lender's quality control plan or self-policing system evidencing appraisal related matters must be provided to the VA office of jurisdiction.

(c) A lender approved to close loans on the automatic basis who subsequently fails to meet the requirements of this section must report the circumstances surrounding the deficiency and the remedial action to be taken to cure it to VA. (Authority: 38 U.S.C. 510(a), 3703(c)(1))

(d) To participate in VA's Automatic Lending Program (ALP) nonsupervised lenders of the class described in paragraph 3702(d)(3) of title 38 U.S. Code shall pay fees as follows:

(1) $500 for new applications;

(2) $200 for reinstatement of lapsed or terminated automatic authority;

(3) $100 for each underwriter approval;

(4) $100 for each agent approval;

(5) $100 for each regional underwriting office approval;

(6) A minimum fee of $100 for any other VA administrative action pertaining to a lender's participation in ALP;

(7) $200 annually for certification of home offices;

(8) $100 annually for certification of regional offices;

(9) $100 annually for each agent renewal.

(e) Supervised lenders of the classes described in paragraphs (d)(1) and (d)(2) of 38 U.S. Code 3702 participating in VA's Loan Guaranty Program shall pay fees as follows:

(1) $100 for each agent approval; and

(2) $100 annually for each agent renewal. (Authority: 38 U.S.C. 501(a) and 3703(c)(1))

(f) Lender participating in VA's Lender Appraisal Processing Program shall pay a fee of $100 for approval of each staff appraisal reviewer.

§36.4349 WITHDRAWAL OF AUTHORITY TO CLOSE LOANS ON THE AUTOMATIC BASIS.

(a) (1) As provided in 38 U.S.C. 3702(e), the authority of any lender to close loans on the automatic basis may be withdrawn by the Secretary at any time upon 30 days notice. The automatic processing of both supervised and nonsupervised lenders may be withdrawn for engaging in practices which are imprudent from a lending standpoint or which are prejudicial to the interests of veterans or the Government but are of a lesser degree than would warrant complete suspension or debarment of the lender from participation in the program.

(2) Automatic processing authority may be withdrawn for failure to meet basic qualifying criteria. For non-supervised lenders, this includes lack of an approved underwriter, failure to maintain $50,000 working capital, and/or failure to file required financial statements. For supervised lenders this includes loss of status as an entity subject to examination and supervision by a Federal or State supervisory agency as required by 38 U.S.C. 3702(d). During the 1 year probationary period for newly-approved nonsupervised automatic lenders, automatic authority may be withdrawn based upon poor underwriting or consistently careless processing by the lender, as determined by VA.

(3) Automatic processing authority may also be withdrawn for any of the causes for debarment set forth at 44.305 of this title.

(b) Authority to close loans on the automatic basis may also be temporarily withdrawn for a period of time under the following schedule.

(1) Withdrawal for 60 days:

(i) Automatic loan submissions show deficiencies in credit underwriting, such as use of unstable sources of income to qualify the borrower, ignoring significant adverse credit items affecting the applicant's creditworthiness, etc., after such deficiencies have been repeatedly called to the lender's attention;

(ii) Employment or deposit verifications are handcarried by applicants or otherwise improperly permitted to pass through the hands of a third party;

(iii) Automatic loan submissions are consistently incomplete after such deficiencies have been repeatedly called to the lender's attention by VA; or

(iv) There are continued instances of disregard of VA requirements after they have been called to the lender's attention.

(2) Withdrawal for 180 days:

(i) Loans are closed automatically which conflict with VA credit standards and which would not have been made by a lender acting prudently;

(ii) The lender fails to disclose to VA significant obligations or other information so material to the veteran's ability to repay the loan that undue risk to the Government results;

(iii) Employment or deposit verifications are allowed to be handcarried by applicant or otherwise mishandled, resulting in the submission of significant misinformation to VA;

(iv) Substantiated complaints are received that the lender misrepresented VA requirements to veterans to the detriment of their interests (e.g., veteran was dissuaded from seeking a lower interest rate based on lender's incorrect advice that such options were precluded by VA requirements);

(v) Closing documentation shows instances of improper charges to the veterans after the impropriety of such charges has been called to the lender's attention by VA, or refusal to refund such charges after notification by VA; or

(vi) There are other instances of lender actions which are prejudicial to the interests of veterans such as deliberate delays in scheduling loan closings.

(3) Withdrawal for a period of from one year to three years:

(i) The lender fails to properly disburse loans (e.g., loan disbursement checks returned due to insufficient funds);

(ii) There is involvement by the lender in the improper use of a veteran's entitlement (e.g., knowingly permitting the veteran to violate occupancy requirements, lender involvement in sale of veteran's entitlement, etc.).

(4) A continuation of actions that have led to previous withdrawal of automatic authority justifies withdrawal of automatic authority for the next longer period of time.

(5) Withdrawal of automatic processing authority does not prevent a lender from processing VA guaranteed loans on the prior approval basis.

(6) Action by VA to remove a lender's automatic authority does not prevent VA from also taking debarment or suspension action based on the same conduct by the lender.

(7) VA field facilities are authorized to withdraw automatic privileges for 60 days, based on any of the violations set forth in paragraphs (b)(1) through (b)(3) of this section, for nonsupervised lenders without operations in other stations' jurisdictions. All determinations regarding withdrawal of automatic authority for longer periods of time or multi-jurisdictional lenders must be made in Central Office.

(c) VA will provide 30 days notice of a withdrawal of automatic authority in order to enable the lender to either close or obtain prior approval for a loan on which processing has begun. There is no right to a formal hearing to contest the withdrawal of automatic processing privileges. However, if within 15 days after receiving notice the lender requests an opportunity to contest the withdrawal, the lender may submit in person, in

writing, or through a representative, information and argument in opposition to the withdrawal.

(d) If the lender's submission in opposition raises a dispute over facts material to the withdrawal of automatic authority, the lender will be afforded an opportunity to appear with a representative, submit documentary evidence, present witnesses, and confront any witnesses VA presents. The Chief Benefits Director will appoint a hearing officer or panel to conduct the hearing.

(e) A transcribed record of the proceedings shall be made available at cost to the lender, upon request, unless the requirement for a transcript is waived by mutual agreement.

(f) In actions based upon a conviction or civil judgment, or in which there is no genuine dispute over material facts, the Chief Benefits Director shall make a decision on the basis of all the information in the administrative record, including any submission made by the lender.

(g) In actions in which additional proceedings are necessary to determine disputed material facts, written findings of fact will be prepared by the hearing officer or panel. The Chief Benefits Director shall base the decision on the facts as found, together with any information and argument submitted by the lender and any other information in the administrative record. (Authority: 38 U.S.C. 501(a), 3703(c)(1))

§36.4350 ESTATE OF VETERAN IN REAL PROPERTY

(a) The estate in the realty acquired by the veteran, wholly or partly with the proceeds of a guaranteed or insured loan, or owned by him or her and on which construction, or repairs, or alterations or improvements are to be made, shall be not less than:

(1) A fee simple estate therein, legal or equitable; or

(2) A leasehold estate running or renewable at the option of the lessee for a period of not less than 14 years from the maturity of the loan, or to any earlier date at which the fee simple title will vest in the lessee, which is assignable or transferable, if the same be subjected to the lien; however, a leasehold estate which is not freely assignable and transferable will be considered an acceptable estate if it is determined by the Chief Benefits Director, or the Director, Loan Guaranty Service, (i) that such type of leasehold is customary in the area where the property is located, (ii) that a veteran or veterans will be prejudiced if the requirement for free assignability is adhered to and, (iii) that the assignability and other provisions applicable to the leasehold estate are sufficient to protect the interests of the veteran and the Government and are otherwise acceptable; or

(3) A life estate, provided that the remainder and reversionary interests are subjected to the lien.

The title to such estate shall be such as is acceptable to informed buyers, title companies, and attorneys, generally, in the community in which the property is situated, except as modified by paragraph (b) of this section.

(b) Any such property or estate will not fail to comply with the requirements of paragraph (a) of this section by reason of the following:

(1) Encroachments;

(2) Easements;

(3) Servitudes;

(4) Reservations for water, timber, or subsurface rights;

(5) Sale and lease restrictions:

(i) Except as to condominiums, the right in any grantor or cotenant in the chain title, or a successor of either, to purchase for cash, which right was established by an instrument recorded prior to December 1, 1976, and by the terms thereof is exercisable only if:

(A) An owner elects to sell,

(B) The option price is not less than the price at which the then owner is willing to sell to another, and

(C) Exercised within 30 days after notice is mailed by registered mail to the address of optionee last known to the then owner of the then owner's election to sell, stating the price and the identity of the proposed vendee;

(ii) A condominium estate established by the filing for record of the Master Deed, or other enabling document before December 1, 1976, will not fail to comply with the requirements of paragraph (a) of this section by reason of:

(A) Prohibition against leasing a unit for a period of less than 6 months.

(B) The existence of a right of first option to purchase or right to provide a substitute buyer reserved to the condominium association provided such option or right is exercisable only if:

(1) An owner elects to sell;

(2) The option price is not less than the price at which the then owner is willing to sell to another,

(3) The terms and conditions under which the option price is to be paid are identical to or are not less favorable to the owner than the terms and conditions under which the owner was willing to sell to the owner's prospective buyer, and

(4) Notice of the association's decision to exercise the option must be mailed to the owner by registered or certified mail within 30 days after notice is mailed by registered or certified mail to the address of the association last known to the owner of the owner's election to sell, stating the price, terms of sale, and the identity of the proposed vendee;

(iii) Any property subject to a restriction on the owner's right to convey to any party of the owner's choice, which restriction is established by a document recorded on or after December 1, 1976, will not qualify as security for a guaranteed or insured loan. A prohibition or restriction on leasing an individual unit in a condominium will not cause

the condominium estate to fail to qualify as security for such loan, provided the restriction is in accordance with §36.4358(c);

(iv) Notwithstanding the provisions of paragraph (b), (5)(i), (ii), and (iii) of this section, a property shall not be considered ineligible pursuant to paragraph (a) of this section if:

(A) The veteran obtained the property under a State or local political subdivision program designed to assist low- or moderate-income purchasers, and as a condition the purchaser must agree to one or more of the following restrictions:

(1) If the property is resold within a time period as established by local law or ordinance, after the purchaser acquires title, the purchaser must first offer the property to the Government housing agency, or a low- or moderate-income purchaser designated by such agency, provided the option to purchase is exercised within 90 days after notice by the purchaser to the agency of intention to sell;

(2) If the property is resold within a time period as established by local law or ordinance after the purchaser acquires title, a governmental agency may specify a maximum price which the veteran may receive for the property upon resale; or

(3) Such other restriction approved by the Secretary designed to insure either that a property acquired under such program again be made available to low- or moderate-income purchasers, or to prevent a private purchaser from obtaining a windfall profit on the resale of such property, while assuring that the purchaser has a reasonable opportunity to dispose of the property without undue difficulty at a reasonable price.

The sale price of a property under any of the restrictions of paragraph (b)(5)(iv)(A) of this section shall not be less than the lowest of the following: The price designated by the owner as the asking price; the appraised value of the property; or the original purchase price of the property, increased by a factor reflecting all or a reasonable portion of the increased costs of housing or the percentage increase in median income in the area between the date of original purchase and resale, plus the reasonable value or actual costs of any capital improvements made by the owner plus a reasonable real estate commission less the cost of necessary repairs required to place the property in saleable condition; or other reasonable formula approved by the Secretary. The veteran must be fully informed and consent in writing to the housing restrictions. A copy of the veteran's consent statement must be forwarded with the application for home loan guaranty or the report of a home loan processed on the automatic basis; or (Authority: 38 U.S.C. 3703(c))

(B) A recorded restriction on title designed to provide housing for older persons, provided that the restriction is acceptable under the provisions of the Fair Housing Act, title VIII of the Civil Rights Act of 1968, as amended by the Fair Housing Amendments Act of 1988, 42 U.S.C. 3601 *et seq*. The veteran must be fully informed and consent in writing to the restrictions. A copy of the veteran's consent statement must be forwarded with the application for home loan guaranty or the report of a home loan processed on the automatic basis; (Authority: 38 U.S.C. 501(a), 3703(c)(1))

(6) Building and use restrictions whether or not enforceable by a reverter clause if there has been no breach of the conditions affording a right to an exercise of the reverter;

(7) Violation of a restriction based on race, color, creed, or national origin, whether or not such restriction provides for reversion or forfeiture of title or a lien for liquidated damages in the event of a breach;

(8) Any other covenant, condition, restriction, or limitation approved by the Secretary in the particular case. Such approval shall be a condition precedent to the guaranty or insurance of the loan;

Provided, That the limitations on the quantum or quality of the estate or property that are indicated in this paragraph, insofar as they may materially affect the value of the property for the purpose for which it is used, are taken into account in the appraisal of reasonable value required by 38 U.S.C., chapter 37.

(c) The following limitations on the quantum or quality of the estate or property shall be deemed for the purposes of paragraph (b) of this section to have been taken into account in the appraisal of residential property and determined by the Secretary as not materially affecting the reasonable value of such property:

(1) *Building or Use Restrictions*. Provided, (i) no violation exists, (ii) the proposed use by a veteran does not presage a violation of a condition affording a right of reverter, and (iii) any right of future modification contained in the building or use restrictions is not exercisable, by its own terms, until at least 10 years following the date of the loan.

(2) *Violations of Racial and Creed Restrictions*. Violations of a restriction based on race, color, creed or national origin, whether or not such restriction provides for reversion or forfeiture of title or a lien for liquidated damages in the event of a breach.

(3) *Violations of Building or Use Restrictions of Record*. Violations of building or use restrictions of record which have existed for more than 1 year, are not the subject of pending or threatened litigation, and which do not provide for a reversion or termination of title, or condemnation by municipal authorities, or, a lien for liquidated damages which may be superior to the lien of the guaranteed or insured mortgage.

(4) *Easements*

(i) Easements for public utilities along one or more of the property lines and easements for drainage or irrigation ditches, provided the exercise of the rights thereof do not interfere with the use of any of the buildings or improvements located on the subject property.

(ii) Mutual easements for joint driveways located partly on the subject property and partly on adjoining property, provided the agreement is recorded in the public records.

(iii) Easements for underground conduits which are in place and which do not extend under any buildings in the subject property.

(5) *Encroachments*

(i) On the subject property by improvements on the adjoining property where such encroachments do not exceed 1 foot within the subject boundaries, provided such encroachments do not touch any buildings or interfere with the use or enjoyment of any building or improvement on the subject property.

(ii) By hedges or removable fences belonging to subject or adjoining property.

(iii) Not exceeding 1 foot on adjoining property by driveways belonging to subject property, provided there exists a clearance of at least 8 feet between the buildings on the subject property and the property line affected by the encroachment.

(6) *Variations of Lot Lines*. Variations between the length of the subject property lines as shown on the plot plan or other exhibits submitted to the Department of Veterans Affairs and as shown by the record or possession lines, provided such variations do not interfere with the current use of any of the improvements on the subject property and do not involve a deficiency of more then 2 percent with respect to the length of the front line or more than 5 percent with respect to the length of any other line. (Authority: 38 U.S.C. 501(a), 3703(c), 3712(g))

§36.4351 LOANS, FIRST, SECOND OR UNSECURED

Loans for the purchase of real property or a leasehold estate as limited in the regulations concerning guaranty or insurance of loans to veterans, or for the alteration, improvement, or repair thereof, and for more than $1,500 and more than 40 percent of the reasonable value of such property or estate prior thereto shall be secured by a first lien on the property or estate. Loans for such alteration, improvement, or repairs for more than $1,500 but 40 percent or less of the prior reasonable value of the property shall be secured by a lien reasonable and customary in the community for the type of alteration, improvement, or repair financed. Those for $1,500 or less need not be secured, and in lieu of the title examination, the lender may accept a statement from the borrower that he or she has an interest in the property not less than that prescribed in §36.4350(a).

§36.4352 TAX, SPECIAL ASSESSMENT AND OTHER LIENS

Tax liens, special assessment liens, and ground rents shall be disregarded with respect to any requirement that loans shall be secured by a lien of specified dignity. With the prior approval of the Secretary, Chief Benefits Director, or Director, Loan Guaranty Service, liens retained by nongovernmental entities to secure assessments or charges for municipal type services and facilities clearly within the public purpose doctrine may be disregarded. In determining whether a loan for the purchase or construction of a home is secured by a first lien the Secretary may also disregard a superior lien created by a duly recorded covenant running with the realty in favor of a private entity to secure an obligation to such entity for the homeowner's share of the costs of the management, operation, or maintenance of property, services or programs within and for the benefit of the development or community in which the veteran's realty is located, if the Secretary determines that the interests of the veteran-borrower and of the Government will not be prejudiced by the operation of such covenant. In respect to any such superior lien to be created after June 6, 1969, the Secretary's determination must have been made prior to the recordation of the covenant.

§36.4353 COMBINATION RESIDENTIAL AND BUSINESS PROPERTY

If otherwise eligible, a loan for the purchase or construction of a combination of residential property and business property which the veteran proposes to occupy in part as a home will be eligible under 38 U.S.C. 3710, if the property is primarily for residential purposes and no more than one business unit is included in the property.

§36.4354 [Reserved]

§36.4355 SUPPLEMENTAL LOANS

(a) Any loan for the alteration, repair, improvement, extension, replacement, or expansion of a home, with respect to which a guaranteed or insured obligation of the borrower is currently outstanding, may be reported for guaranty or insurance coverage, if such loan is made by the holder of the currently outstanding obligation, notwithstanding the fact no guaranty entitlement remains available to the borrower:

Provided, That if no entitlement remains available the maximum amount payable on the revised guaranty shall not exceed the amount payable on the original guaranty on the date of closing the supplemental loan, and the percentage of guaranty shall be based upon the proportion the said maximum amount bears to the aggregate indebtedness, or, in the case of an insured loan, no additional credit to the holder's insurance account may be made: *Provided further*, That the prior approval of the Secretary shall be required if

(1) The loan will be made by a lender who is not the holder of the currently guaranteed or insured obligation; or

(2) The loan will be made by a lender not of a class specified in 38 U.S.C. 3702(d); or

(3) An obligor liable on the currently outstanding obligation will be released from personal liability.

In any case in which the unpaid balance of the prior loan currently outstanding is combined or consolidated with the amount of the supplemental loan, the entire aggregate indebtedness shall be repayable in full within the maximum maturity currently prescribed by statute for the original loan. No supplemental loan for the repair, alteration, or improvement of residential property will be eligible for guaranty or insurance unless such repair, alteration, or improvement substantially protects or improves the basic livability or utility of the property involved.

(b) Such loan shall be secured as required in §36.4351: *Provided*, That a lien of lesser dignity than therein specified will suffice if the lien obtained is immediately junior to the lien of the original guaranteed or insured obligation: *Provided further*, The liens of successive supplemental loans may be of lesser dignity so long as they are immediately junior to the lien of the last previous guaranteed or insured obligation having a lien of required dignity.

(c) Upon providing or extending guaranty or insurance coverage in respect to any such supplemental loan, the rights of the Secretary to the proceeds of the sale of security shall be subordinate to the right of the holder to satisfy therefrom the indebtedness outstanding on the original and supplemental loans.

§36.4356 CONDOMINIUM LOANS-GENERAL

(a) *Authority-Applicability of Other Loan Guaranty Regulations 38 CFR, Part 36.* A loan to an eligible veteran to purchase a one-family residential unit in a condominium housing development or project shall be eligible for guaranty or insurance to the same extent and on the same terms as other loans under 38 U.S.C. 3710 provided the loan conforms to the provisions of chapter 37, title 38, U.S.C., except for sections 3711 (direct loans), and 3727 (structural defects). The loan must also conform to the otherwise applicable provisions of the regulations concerning the guaranty or insurance of loans to veterans. Sections 36.4353, 36.4355, and 36.4364 shall not be applicable.

(b) *Definitions*. On and after July 1, 1979, the following definitions shall be applicable to each condominium loan entitled to be guaranteed or insured, and shall be applicable to such loans previously guaranteed or insured to the extent that no legal rights vested thereunder are impaired. Whenever used in 38 U.S.C., chapter 37 or the §36.4300 series, unless the context otherwise requires, the terms defined in this paragraph shall have the meaning stated.

(1) *Affiliate of Declarant*. Affiliate of declarant means any person or entity which controls, is controlled by, or is under common control with, a declarant.

(i) A person or entity shall be considered to control a declarant if that person or entity is a general partner, officer, director, or employee of the declarant who:

(a) Directly or indirectly or acting in concert with one or more persons, or through one or more subsidiaries, owns, controls, or holds with power to vote, or holds proxies representing, more than 20 percent of the voting shares of the declarant;

(b) Controls in any manner the election of a majority of the directors of the declarant; or

(c) Has contributed more than 20 percent of the capital of the declarant.

(ii) A person or entity shall be considered to be controlled by a declarant if the declarant is a general partner, officer, director, or employee of that person or entity who:

(a) Directly or indirectly or acting in concert with one or more persons or through one or more subsidiaries, owns, controls, or holds with power to vote, or holds proxies representing, more than 20 percent of the voting shares of that person or entity;

(b) Controls in any manner the election of a majority of the directors of that person or entity; or

(c) Has contributed more than 20 percent of the capital of that person or entity.

(2) *Condominium*. Unless otherwise provided by State law, a condominium is a form of ownership in which the buyer receives title to a three dimensional air space containing the individual living unit together with an undivided interest or share in the ownership of common elements (restatement of §36.4301, Condominium.)

(3) *Conversion Condominium*. Condominium projects not originally built and sold as condominiums but subsequently converted to condominium form of ownership.

(4) *Declarant*. Any person who has executed a declaration or an amendment to a declaration to add additional real estate to the project, or any successors or assigns of the declarant who offers to sell or sells units in the condominium project and who assumes declarant rights in the project including the right to: Add, convert or withdraw real estate from the condominium project; maintain sales offices, management offices and rental units; exercise easements through the common elements for the purpose of making improvements within the condominium; or exercise control of the owners' association. Declarant is further defined as any sponsor of a project or affiliate of the declarant who is acting on behalf of or exercising the rights of the declarant.

(5) *Existing-Declarant in Control or Marketing Units*. A condominium in which all onsite or offsite improvements were completed or the conversion was completed prior to appraisal by the Department of Veterans Affairs, but the declarant is in control of the owners' association and/or is currently marketing units for initial transfer to individual unit owners.

(6) *Existing-Resale*. A condominium in which all onsite or offsite improvements were completed or the conversion was completed prior to appraisal by the Department of Veterans Affairs, and the declarant is no longer in control of the owners' association and/or marketing units for initial transfer to individual unit owners.

(7) *Expandable Condominium*. A project which may be increased in size by the declarant. An expandable condominium is constructed in phases (or stages). After each phase is completed and constituted, the common estates are merged. Each unit owner, thereby, gains an individual interest in all of the facilities of the common estate.

(8) *Foreclosure*. Foreclosure shall mean the termination of a lien by either judicial or nonjudicial procedures in accordance with local law or the voluntary transfer of property by a deed-in-lieu of foreclosure or similar procedures.

(9) *High Rise Condominium*. A condominium project which is a multi-story elevator building.

(10) *Horizontal Condominium*. A condominium project in which generally no part of a living unit extends over and under another living unit.

(11) *Low Rise Condominium*. A condominium project in which all or a part of a living unit extends over or under another living unit; e.g., garden apartment or walk-up project.

(12) *Proposed Condominium*. A condominium project that is to be constructed or is under construction. In the case of a condominium conversion, the declarant proposes to convert a building or buildings to the condominium form of ownership, or the declarant is in the process of converting the building or buildings to the condominium form of ownership.

(13) *Series Condominium*. A number of adjoining but separately constituted condominiums. As association of owners is established for each project, and each association is responsible for maintenance and upkeep of the common elements in its own project. Cross-easements between the separate condominiums may be created to permit members of the separate condominiums to use the common areas of the other condominiums.

(c) *Project Approval*. Prior to the Department of Veterans Affairs guaranty of an individual unit loan in a condominium, the legal documentation establishing the condominium project or development must be approved by the Secretary. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

§36.4357 ACCEPTABLE OWNERSHIP ARRANGEMENTS AND DOCUMENTATION

(a) *Types of Condominium Ownership*. The following types of basic ownership arrangements are generally acceptable provided they are established in compliance with

the applicable condominium law of the jurisdiction(s) in which the condominium is located:

(1) Ownership of units by individual owners coupled with an undivided interest in all common elements.

(2) Ownership of units by individual owners coupled with an undivided interest in general common elements and specified limited common elements.

(3) Individual ownership of units coupled with an undivided interest in the general common elements and/or limited common elements, with title to additional property for common use vested in an association of unit owners, with mandatory membership by unit owners or owners' associations. Any such arrangement must not be precluded by applicable State law. (Authority: 38 U.S.C. 510(b), 3710(a)(6))

(b) *Estate of Unit Owner.* The legal estate of each unit owner must comply with the provisions of §36.4350. The declaration or equivalent document shall allocate an undivided interest in the common elements to each unit. Such interest may be allocated equally to each unit, may be proportionate to that unit's relative size or value, or may be allocated according to any other specified criteria provided that the method chosen is equitable and reasonable for the condominium. (Authority: 38 U.S.C. 510(b), 3703(c)(1), (d)(3), 3710(a)(6))

(c) *Condominium Documentation*

(1) *Compliance with Applicable Law*. The declaration, bylaws and other enabling documentation shall conform to the laws governing the establishment and maintenance of condominium regimes within the jurisdiction in which the condominium is located, and to all other laws which apply to the condominium.

(2) *Recordation*. The declaration and all amendments or modifications thereof shall be placed of record in the manner prescribed by the appropriate jurisdiction. If recording of plats, plans, or bylaws or equivalent documents and all amendments or modifications thereof is the prevailing practice or is required by law within the jurisdiction where the project is located, then such documents shall be placed of record. If the bylaws are not recorded, then covenants, restrictions and other matters requiring record notice should be contained in the declaration or equivalent document.

(3) *Availability*. The owners' association shall be required to make available to unit owners, lenders and the holders, insurers and guarantors of the first mortgage on any unit, current copies of the declaration, bylaws and other rules governing the condominium, and other books, records and financial statements of the owners' association. The owners' association also shall be required to make available to prospective purchasers current copies of the declaration, bylaws, other rules governing the condominium, and the most recent annual audited financial statement, if such is prepared. "Available" as used in this paragraph (c)(3) shall at least mean available for inspection, upon request, during normal business hours or under other reasonable circumstances.

(4) *Amendments to Documents After Department of Veterans Affairs Project Approval.* While the declarant is in control of the owners' association, amendments to the declaration, bylaws or other enabling documentation must be approved by the Secretary. The declarant should have proposed amendments reviewed prior to recordation. This provision does not apply to amendments which annex additional phases to the

condominium regime in accordance with a general plan of development. (§36.4360(a)(3) and §36.4360a(b)(6).). (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

(d) *Real Property Descriptions in the Declaration*

(1) *Clarity-Conformity with the Law of the Jurisdiction*. The description of the units, common elements, any recreational facilities and other related amenities, and any limited common elements shall be clear and in conformity with the law of the jurisdiction where the project is located. Responsibility for maintenance and repair of all portions of the condominium shall be set forth clearly.

(2) *Developmental Plan-Proposed Condominiums*. The declaration or other legally enforceable and binding document must state in a reasonable manner the overall development plan of the condominium, including building types, architectural style and the size of the units for those phases of the condominium which are required to be built. Under the applicable provisions of the declaration or such other legally enforceable and binding document, the development of the required portion of the condominium must be consistent with the overall plan, except that the declarant may reserve the right to change the overall plan or decide not to construct planned units or improvements to the common elements if the declaration sets forth the conditions required to be satisfied prior to the exercise of that right the time within which the right may be exercised, and any other limitations and criteria that would be necessary or appropriate under the particular circumstances. Such conditions, time restraints and other limitations must be reasonable in light of the overall plan for the condominium. In an expandable project, additional phases which are not required to be built may be described in the development plan in very general terms, or the declaration may provide that the declarant makes no assurances concerning the construction, building types, architectural style and size of the units, etc., of these phases. However, the minimum number of units to be built should be that which would be adequate to reasonably support the common elements. (See §36.4360(a)(6).) (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

§36.4358 RIGHTS AND RESTRICTIONS

(a) *Declarant's Rights and Restrictions*

(1) *Disclosure and Reasonableness of Reserved Rights.* Any right reserved by the declarant must be reasonable and set forth in the declaration.

(2) *Examples of Reserved Rights of Declarant, Sponsor, or Affiliate of Declarant which are Usually Unacceptable*. Binding the owners' association either directly or indirectly to any of the following agreements is not acceptable unless the owners' association shall have a right of termination thereof which is exercisable without penalty at any time after transfer of control, upon not more than 90 days' notice to the other party thereto:

(i) Any management contract, employment contract or lease of recreational or parking areas or facilities;

(ii) Any contract or lease, including franchises and licenses, to which a declarant is a party.

The requirements of paragraphs (a)(2)(i) and (ii) of this section do not apply to acceptable ground leases.

(3) *Examples of Reserved Rights which are Usually Acceptable*. The following rights in the common elements may usually be reserved by the declarant for a reasonable period of time, subject to a concomitant obligation to restore:

(i) Easement over and upon the common elements and upon lands appurtenant to the condominium for the purpose of completing improvements for which provision is made in the declaration, but only if access thereto is otherwise not reasonably available.

(ii) Easement over and upon the common elements for the purpose of making repairs required pursuant to the declaration or contracts of sale made with unit purchasers.

(iii) Right to maintain facilities in the common areas which are identified in the declaration and which are reasonably necessary to market the units. These may include sales and management offices, model units, parking areas, and advertising signs. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

(b) *Owners' Association's Rights and Restrictions*

(1) *Right of Entry Upon Units and Limited Common Elements*. The owners' association shall be granted a right of entry upon unit premises and any limited common elements to effect emergency repairs, and a reasonable right of entry thereupon to effect other repairs, improvements, replacement or maintenance as necessary.

(2) *Power to Grant Rights and Restrictions in Common Elements.* The owners' association should be granted other rights, such as the right to grant utility easements under, through or over the common elements, which are reasonably necessary to the ongoing development and operation of the project.

(3) *Responsibility for Damage to Common Elements and Units.* A provision may be made in the declaration or bylaws for allocation of responsibility for damages resulting from the exercise of any of the above rights.

(4) *Assessments.*

(i) *Levy and Collection*. The declaration or its equivalent shall describe the authority of the owners' association to levy and enforce the collection of general and special assessments for common expenses and shall describe adequate remedies for failure to pay such common expenses. The common expenses assessed against any unit, with interest, late charges, costs and a reasonable attorney's fee shall be a lien upon such unit in accordance with applicable law. Each such assessment, together with interest, late charges, costs, and attorney's fee, shall also be the personal obligation of the person who was the owner of such unit at the time the assessment fell due. The personal obligation for delinquent assessments shall not pass to successors in title or interest unless assumed by them, or required by applicable law. Common expenses as used in this subdivision shall mean expenditures made or liabilities incurred by or on behalf of the owners' association, together with any assessments for the creation and maintenance of reserves.

(ii) *Reserves and Working Capital*. There shall be in new or proposed condominium projects (including conversions) a provision for an adequate reserve fund for the periodic maintenance, repair and replacement of the common elements, which fund shall be maintained out of regular assessments for common expenses. Additionally, a working capital fund must be established for the initial months of the project operations equal to at least 2 months' estimated common area charge for each unit.

(iii) *Priority of Lien.* Any assessment lien must be subordinate to any Department of Veterans Affairs guaranteed mortgage except as provided in §36.4352. A lien for common expense charges and assessments shall not be affected by any sale or transfer of a unit except that a sale or transfer pursuant to a foreclosure of a first mortgage shall extinguish a subordinate lien for common expense charges and assessments which became payable prior to such sale or transfer. Any such sale or transfer pursuant to a foreclosure shall not relieve the purchaser or transferee of a unit from liability for, nor the unit so sold or transferred from the lien of, any common expense charges thereafter becoming due. (Authority: 38 U.S.C. 501(b), 3703(c)(1), (d)(3), 3710(a)(6))

(c) *Unit Owners' Rights and Restrictions.*

(1) *Obligation to Pay Expenses.* The declaration or equivalent document shall establish a duty on each unit owner, including the declarant, to pay a proportionate share of common expenses upon being assessed therefor by the owners' association. Such share may be allocated equally to each unit, may be proportionate to that unit's common element interest, relative size or value, or may be allocated according to any other specified criteria provided that the method chosen is equitable and reasonable for that condominium.

(2) *Voting Rights.* The declaration or equivalent document shall allocate a portion of the votes in the association to each unit. Such portion may be allocated equally to each unit, may be proportionate to that unit's common expense liability, common element interest, relative size or value, or may be allocated according to any other specified criteria provided that the method is equitable and reasonable for the condominium. The declaration may provide different criteria for allocations of votes to the units on particular specified matters and may also provide different percentages of required unit owner approvals for such particular specified matters.

(3) *Ingress and Egress of Unit Owners.* There may not be any restriction upon any unit owner's right of ingress and egress to his or her unit.

(4) *Encroachment - Units and Common Elements.*

(i) *Easements for Encroachments.* In the event any portion of the common elements encroaches upon any unit or any unit encroaches upon the common elements or another unit as a result of the construction, reconstruction, repair, shifting, settlement, or movement of any portion of the improvements, a valid easement for the encroachment and for the maintenance of the same shall exist so long as the encroachment exists. The declaration may provide, however, reasonable limits on the extent of any easement created by the overlap of units, common elements, and limited common elements resulting from such encroachments; or

(ii) *Monuments as Boundaries*. If permitted by the governing law within the jurisdiction where the project is located, the existing physical boundaries of a unit or a common element of the physical boundaries of a unit or a common element reconstructed in substantial accordance with the original plats and plans thereof become its boundaries rather than the metes and bounds expressed in the deed, plat or plan, regardless of settling or lateral movement of the building, or minor variance between boundaries should on the plats, plans or in the deed and those of the building. The declaration should provide reasonable limits on the extent of any such revised boundary(ies) created by the overlap

of units, common elements, and limited common elements resulting from such encroachments.

(5) *Right of First Refusal*. The right of a unit owner to sell, transfer, or otherwise convey his or her unit in a condominium shall not be subject to any right of first refusal or similar restriction if the declaration or similar document is recorded on or after December 1, 1976. If the declaration was recorded prior to December 1, 1976, the right of first refusal must comply with §36.4350(b)(5)(ii); *Provided, however*, restrictions on the basis of age or restrictions established by a State, Territorial, or local government agency as part of a program for providing assistance to low- and moderate-income purchasers shall be governed by §36.4350(b)(5)(iv). (Authority: 38 U.S.C. 3703(c))

(6) *Leasing Restrictions*. Except as provided in this paragraph, there shall be no prohibition or restriction on a condominium unit owner's right to lease his or her unit. The following restrictions are acceptable:

(i) A requirement that leases have a minimum initial term of up to 1 year, or

(ii) Age restrictions or restrictions imposed by State or local housing authorities which are allowable under §36.4308(e) or §36.4350(b)(5)(iv).

(d) *Rights of Action*. The owners' association and any aggrieved unit owner should be granted a right of action against unit owners for failure to comply with the provisions of the declaration, bylaws, or equivalent documents, or with decisions of the owners' association which are made pursuant to authority granted the owners' association in such documents. Unit owners should have similar rights of action against the owners' association. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

§36.4359 MISCELLANEOUS LEGAL REQUIREMENTS

(a) *Declarant Transfer of Control of Owners' Association.*

(1) *Standards for Transfer of Control*. The declarant shall relinquish all special rights, expressed or implied, through which the declarant may directly or indirectly control, direct, modify, or veto any action of the owners' association, its executive board, or a majority of unit owners, and control of the owners' association shall pass to the owners of units within the project, not later than the earlier of the following:

(i) 120 days after the date by which 75 percent of the units have been conveyed to unit purchasers, or

(ii) The last date of a specified period of time following the first conveyance to a unit purchaser; such period of time is to be reasonable for the particular project. The maximum acceptable period usually will be from 3 to 5 years for single-phased condominium regimes and 5 to 7 years for expandable condominiums.

(iii) On a case basis, modifications or variations of the requirements of paragraphs (a)(i) and (ii) of this section (a)(1) will be acceptable, particularly in circumstances involving very large condominium developments.

(2) *Declarant's Unit Votes after Transfer of Control.* The requirements of paragraph (a)(1) of this section shall not affect the declarant's rights, as a unit owner, to exercise the votes allocated to units which declarant owns.

(3) *Unit Owners' Participation in Management*. Declarants should provide for and foster early participation of unit owners in the management of the project.

(b) *Taxes*. Unless otherwise provided by State law, real estate taxes must be assessed and be lienable only against the individual units, together with their undivided interests in the common elements, and not against the multifamily structure. The owners' association usually owns no real estate, so it has no obligation concerning ad valorem taxes. Unless taxes are assessed only against the individual units, a tax lien could amount to more than the value of any particular unit in the structure.

(c) [Reserved.]

(d) *Policies for Bylaws*. The bylaws of the condominium should be sufficiently detailed for the successful governance of the condominium by unit owners. Among other things, such documents should contain adequate provisions for the election and removal of directors and officers.

(e) *Insurance and Related Requirements*

(1) *Insurance*. The holder shall require hazard and flood insurance policies to be procured and maintained in accordance with §36.4326. Because of the nature of condominiums, additional types of insurance coverages-such as tort liability insurance for injuries sustained on the premises, personal liability insurance for directors and officers managing association affairs, boiler insurance, etc. should be considered in appropriate circumstances.

(2) *Fidelity Bond Coverage*. The securing of appropriate fidelity bond coverage is recommended but not required, for any person or entity handling funds of the owners' association, including, but not limited to, employees of the professional managers. Such fidelity bonds should name the association as an obligee, and be written in an amount equal to at least the estimated maximum of funds, including reserve funds, in the custody of the owners' association or the management agent at any given time during the term of the fidelity bond. However, the bond should not be less than a sum equal to 3 months' aggregate assessments on all units plus reserve funds. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

§36.4360 DOCUMENTATION AND RELATED REQUIREMENTS-FLEXIBLE CONDOMINIUMS AND CONDOMINIUMS WITH OFFSITE FACILITIES

(a) *Expandable Condominiums*. The following policies apply to condominium regimes which may be increased in size by the declarant:

(1) The declarant's right to expand the regime must be fully described in the declaration. The declaration must contain provisions adequate to ensure that future improvements to the condominium will be consistent with initial improvements in terms of quality of construction. The declarant must build each phase in accordance with an approved general plan for the total development (§36.4357(d)(2)) supported by detailed plats and plans of each phase prior to the construction of the particular phase.

(2) The reservation of a right to expand the condominium regime, the method of expansion and the result of an expansion must not affect the statutory validity of the condominium regime or the validity of title to the units.

(3) The declaration or equivalent document must contain a covenant that the condominium regime may not be amended or merged with a successor condominium regime without prior written approval of the Secretary. The declarant may have the proposed legal documentation to accomplish the merger reviewed prior to recordation. However, the Secretary's final approval of the merger will not be granted until the successor condominium has been legally established and construction completed. The declarant may add phases to an expandable condominium regime without the prior approval of the Secretary if the phasing implements a previously approved general plan for the total development. A copy of the amendment to the declaration or other annexation document which adds each phase must be submitted to the Secretary in accordance with §36.4360a(b)(6).

(4) Liens arising in connection with the declarant's ownership of, and construction of improvements upon, the property to be added must not adversely affect the rights of existing unit owners, or the priority of first mortgages on units in the existing condominium property. All taxes, assessments, mechanic's liens, and other charges affecting such property, covering any period prior to the addition of the property, must be paid or otherwise satisfactorily provided for by the declarant.

(5) The declarant must purchase (at declarant's own expense) a general liability insurance policy in an amount not less than $1 million for each occurrence, to cover any liability which owners of previously sold units are exposed to as a result of further condominium development.

(6) Each expandable project shall have a specified maximum number of units which will give each unit owner a minimum percentage of interest in the common elements. Each project shall also have a specified minimum number of units which will give each unit owner a maximum percentage of interest in the common elements. The minimum number of units to be built should be that which would be adequate to reasonably support the common elements. The maximum number of units to be built should be that which would not overload the capacity of the common facilities. The maximum possible percentage(s) and the minimum possible percentage(s) of undivided interest in the common elements for each type of unit must be stated in the declaration or equivalent document.

(7) The declaration or equivalent document shall set forth clearly the basis for reallocation of unit owner's ownership interests, common expense liabilities and voting rights in the event the number of units in the condominium is increased. Such reallocation shall be according to the applicable criteria set forth in §§36.4357(b) and 36.4358(c)(1) and (2).

(8) The declarant's right to expand the condominium must be for a reasonable period of time with a specific ending date. The maximum acceptable period will usually be from 5 to 7 years after the date of recording the declaration. On a case bases, longer periods of expansion rights will be acceptable, particularly in circumstances involving sizable condominium developments.

(b) *Series Projects.*

(1) Each phase in the series approach is to be considered as a separate project. A separate set of legal documents must be filed for each phase or project that relates to the condominium within its own boundary. The declaration for each phase must describe the particular project as a part of the whole development area, but subject only the one phase

to the condominium regime. A separate unit ratio must be established that would relate each unit to all units of the particular condominium for purposes of ownership in the common areas, voting rights and assessment liability. A separate association may be created to govern the affairs of each condominium. Each phase is subject to a separate presale requirement.

(2) In the case of proposed projects, or projects under construction, the declaration should state the number of total units that the developer intends to build on other sections of the development area.

(c) *Other Flexible Condominiums*. Condominiums containing withdrawable real estate (contractable condominiums) and condominiums containing convertible real estate (portions of the condominium within which additional units or limited common elements, or both, may be created) will be considered acceptable provided the flexible condominium complies with the §36.4300 series. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

§36.4360a APPRAISAL REQUIREMENTS

(a) *Existing Resale Condominiums*. Upon acceptance by the local office of the organizational documents, the project and unit(s) proposed as security for guaranteed financing shall be appraised to ensure that they meet MPR's (Minimum Property Requirements) and are safe, sanitary, and structurally sound. The Department of Veterans Affairs MPR's for existing construction apply to all existing resale condominiums including conversions, except that water, heating, ventilating, air-conditioning and sewer service may be supplied from a central source. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6), (b)(5))

(b) *Proposed Condominiums or Existing Condominiums with Declarant in Control or Marketing Units.*

(1) *Low Rise and High Rise Condominiums*. Low rise and high rise condominiums shall comply with local building codes. Only the alterations, improvements or repairs to low rise and high rise buildings proposed to be converted to the condominium form of ownership must comply with current local building codes, unless local authorities require total code compliance on the entire structure when a building is being converted to the condominium form of ownership. In those areas where local standards are nonexistent, inferior to, or in conflict with the Department of Veterans Affairs objectives, a certification will be required from a registered professional architect and/or registered engineer certifying that the plans and specifications conform to one of the national building codes which is typical of similar construction methods and standards for condominiums used in the area. Those portions of the condominium conversion which are not being altered, improved or repaired must be appraised in accordance with paragraph (a) of this section.

(2) *Horizontal Condominiums*. Department of Veterans Affairs policies and procedures applicable to single-family residential construction shall also apply to horizontal condominiums. Proposed or existing (declarant in control or marketing units) horizontal condominium conversions shall comply with current local building codes for alterations and improvements or repairs made to convert the building to the condominium form of ownership unless local authorities require total code compliance on the entire structure when a building is being converted to the condominium form of ownership. In those areas where local standards are nonexistent, inferior to, or in conflict with Department of Veterans Affairs objectives, a certification will be required from a

professional architect and/or registered engineer certifying that the plans and specifications conform to one of the national building codes which is typical of similar construction methods and standards for condominiums used in the area. Those portions of the condominium conversion which are not being altered, improved or repaired must be appraised in accordance with paragraph (a) of this section. (Authority: 38 U.S.C. 501(b), 3703(c)(1))

(3) *Unit Completion*. All units in the individual project or phase must be substantially completed except for customer preference items, such as interior finishes, appliances or equipments.

(4) *Common Element Completion*. All amenities of the condominium (to include offsite community facilities), that are to be considered in the unit value, must be bound legally to the condominium regime. All such amenities as well as the common elements of the project, must be substantially completed and available for use by the unit owners. In large multi-phase projects, the declarant should construct common elements in a manner consistent with the addition of units to support the entire development. The Secretary, in appropriate cases, may approve the placement of adequate funds by the declarant in an escrow or otherwise earmarked account or accept a letter of credit or surety bond to assure completion of amenities and allow closing of VA-guaranteed (or insured) loans. Such funds must be adequate to assure completion of the amenities free and clear of all liens. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

(5) *Information Brochure/Public Offering Statement*. When units are being sold by the declarant (not applicable to resales), and information brochure/public offering statement must be given to veteran buyers prior to the time a downpayment is received and an agreement is signed, unless State law authorized receipt of the downpayment and delivery of the information brochure followed by a period in which purchasers may cancel the purchase agreement without penalty for a specified number of days. Information brochures must be written in simple terms to inform buyers that the association does not provide owner's contents and personal liability policies which are the owner's responsibility. In the event the development is expandable, series, etc., there must be full disclosure of the impact of the total development plan. In expandable, series or other projects with more than one phase, the information brochure must disclose fully later development rights, and the general plans of the declarant for additional phases. If the declarant makes no assurance concerning phases which are not required to be built, the declarant should state that no assurances are given concerning construction, unit sizes, building types, architectural styles, etc. In condominium conversions, the information brochure must list the major structural and mechanical components and the estimated remaining useful life of the components. A brief explanation must be furnished in the brochure explaining that certain major structural or mechanical components may require replacement within a specified time period. If the declarant has elected to place funds into a condominium reserve fund for replacement of a major component under the provisions of §36.4360a(b)(7), the amount of the contribution into the reserve fund must be specified in the information brochure.

(6) *Evidence of Proper Phasing*. In an expandable or flexible condominium, evidence of the addition of each phase in accordance with a previously approved general plan of development must be submitted to the Secretary prior to the guaranty of the first loan in the added area.

(7) *Additional Condominium Conversion Requirements.*

(i) The declarant of a condominium project, which is (A) proposed, (B) under construction, or (C) an existing project with a declarant in control or marketing units not previously occupied, must furnish structural and mechanical common element component statements on the present condition of all accessible structural and mechanical components material to the use and enjoyment of the condominium. These statements must be completed by a registered professional engineer and/or architect prior to the guaranty of the first unit loan in the project. Each statement must also give an estimate of the expected useful life of the roof, elevators, heating and cooling, plumbing and electrical systems assuming normal maintenance. A minimum of 10 years estimated remaining useful life is required on all structural and mechanical components. In the alternative, the declarant may contribute an amount of funds to the condominium reserve fund equal to a minimum of 1/10 (one-tenth) of the estimated costs of replacement of a major structural or mechanical component (as determined by an independent registered professional architect or engineer) for each year of estimated remaining useful life less than 10 years; e.g., 7 years remaining useful life equals a 3/10 required declarant contribution to the reserve fund of the component's estimated replacement cost. The noted statements and remaining useful life requirement are not applicable to existing resale conversion projects when the declarant is no longer marketing units and/or in control of the association. Expandable or series condominium conversions require engineering and architectural statements on each stage or phase.

(ii) In declarant controlled projects, a statement(s) by the local authority(ies) of the adequacy of offsite utilities servicing the site (e.g., sanitary or water) is required. If a local authority(ies) declines to issue such a statement(s), a statement(s) may be obtained from a registered professional engineer.

(c) *Presale Requirements.*

(1) *Proposed Construction or Existing Declarant in Control*. Bona fide agreements of sale must have been executed by purchasers other than the declarant (who are obligated contractually to complete the purchase) of 70 percent of the total number of units in the project. Lenders shall certify as to satisfaction of the presale requirement prior to VA guaranty of the first unit loan. When a declarant can demonstrate that a lower percentage would be justified, the Secretary, on an individual case basis, may approve a presale requirement of less than 70 percent. Reduction of the 70 percent presale requirement will be considered when:

(i) Strong initial sales demonstrate a ready market, or

(ii) The declarant will provide cash assets or acceptable bonds for payment of full common area assessments to the owners' association until such assessments are assumed by unit purchasers, or

(iii) Subsequent phases of an overall development are being undertaken in a proven market area, or

(iv) Previous experience in similar projects in the same market area indicates strong market acceptance, or

(v) The development is in a market area that has repeatedly indicated acceptance of such projects.

(2) *Multiphase-Proposed or Existing Declarant in Control*. The requirements of paragraph (c)(1) of this section shall apply to each individual phase of a multiphase

development, taking into consideration that each individual phase must be capable of self-support in the event that the developer does not complete all planned phases.

(d) *Warranty*. Except in condominium conversion projects, each CRV (certificate of reasonable value) issued by the Secretary relating to a proposed or existing not previously occupied dwelling unit in a condominium project shall be subject to the express condition that the builder, seller, or the real party in interest in the transaction shall deliver to the veteran purchasing the dwelling unit with the aid of a guaranteed or insured loan a warranty against defects for the unit and common elements. The unit shall be warranted for 1 year from the date of settlement or the date of occupancy (whichever first occurs). The common elements shall be warranted for 2 years from the date each of the common elements is completed and available for use by the unit owners, or 2 years from the date the first unit is conveyed to a unit owner other than the declarant, whichever is later, in the particular phase of the condominium containing the common element. For these purposes, defects shall be those items reasonably requiring the repair, renovation, restoration, or replacement of any of the components constituting the unit or common elements. Items of maintenance relating to the unit or common elements are not covered by the warranty. No certificate of guaranty or insurance credit shall be issued unless a copy of such warranty, duly receipted by the purchaser, is submitted with the loan papers.

(e) *Ownership and Operation of Offsite Facilities.*

(1) *Title Requirements*. Evidence must be presented that the offsite facility owned by an owners' association with mandatory membership by condominium unit owners or condominium unit owners' associations has been completed and conveyed free of encumbrances by the declarant for the benefit of the unit owners with title insured by an owner's title policy or other acceptable title evidence. Offsite facilities conveyed to a nonprofit corporation are the preferred method of offsite facilities ownership; however, the Secretary will consider other forms of ownership on an individual case basis.

(2) *Mandatory Membership*. The declaration of the condominium (each condominium in a series development) and the legal documentation of the corporation or association which owns the offsite facility must provide the following:

(i) The owner of a condominium unit is automatically a member of the offsite facility corporation or association and that upon the sale of the unit, membership is transferred automatically to the new owner/purchaser. It is also acceptable if each condominium owners' association (in lieu of each individual unit owner) is automatically a member of the offsite facility corporation or association coupled with use rights for each of the unit owners or residents. If membership in an offsite owners' association is voluntary, no credit in the CRV valuation may be given for such offsite amenities.

(ii) Each member of the offsite facility corporation or association must be entitled to a representative vote at meetings of the offsite facility corporation or association. If the individual condominium owners' association is a member of the offsite facility corporation or association, each condominium owners' association must be entitled to a representative vote at meetings of the offsite facility corporation or association.

(iii) Each member must agree by acceptance of the unit deed to pay a share of the expenses of the offsite facility corporation or association as assessed by the corporation or association for upkeep, insurance, reserve fund for replacements, maintenance and operation of the offsite facility. The share of said expenses shall be determined equitably. Failure to pay such assessment must result in a lien against the individual unit

in the same manner as unpaid assessments by the owners' association of the condominium. If each condominium owners' association is a member of the offsite facility in lieu of individual unit owners failure of the condominium owners' association to pay its equitable assessment to the offsite facility must result in an enforceable lien.

(3) *Declarant Payment of Offsite Facility in a Series Project*. Until the declarant has completed all of the intended condominium phases in a total condominium development or established each condominium regime by filing a separate declaration in a series development, the balance of the total sum of the expenses of the offsite facility not covered by the assessment against the unit owners should be assessed against and be payable by the declarant commencing on the first day of the first month after the first unit is conveyed to a homeowner in the first phase. If this balance is not paid, it must become a lien against those parcels of land in the development area which are owned by the declarant. The collection of such debt and enforcement of such lien may be by foreclosure or such other remedies afforded the corporation or association under local law.

(f) *Professional Management*. Many condominiums are small enough and their common areas so minimal that professional management is not necessary. VA does not have a requirement for professional management of condominiums. The powers given to the owners' association by the declaration and bylaws are fundamentally for "use control" and maintenance of the undivided interest all of the owners have in the common areas. These powers normally include management which may, if desired, be delegated to a professional manager. However, if the board of directors wants professional management, the management agreement must be terminable for cause upon 30 days' notice, and run for a reasonable period of from 1 to 3 years and be renewable by consent of the association and management. (Management contracts negotiated by the declarant should not exceed 2 years.)

(g) *Commercial Areas*. With respect to existing and proposed condominiums, commercial areas within condominium developments are acceptable, but such interests will be considered in value. (Authority: 38 U.S.C. 501(b), 3703(c)(1), 3710(a)(6))

§36.4362 REQUIREMENT OF CONSTRUCTION WARRANTY

Each certificate of reasonable value issued by the Secretary relating to a proposed or newly constructed dwelling unit, except those covering one-family residential units in condominium housing developments or projects within the purview of §36.4356 through §36.4360a, shall be subject to the express condition that the builder, seller, or the real party in interest in the transaction shall deliver to the veteran constructing or purchasing such dwelling with the aid of a guaranteed or insured loan a warranty, in the form prescribed by the Secretary, that the property has been completed in substantial conformity with the plans and specifications upon which the Secretary based the valuation of the property, including any modifications thereof, or changes or variations therein, approved in writing by the Secretary, and no certificate of guaranty or insurance credit shall be issued unless a copy of such warranty duly receipted by the purchaser is submitted with the loan papers.

§36.4363 NONDISCRIMINATION AND EQUAL OPPORTUNITY IN HOUSING CERTIFICATION REQUIREMENTS

(a) Any request for a master certificate of reasonable value on proposed or existing construction, and any request for appraisal of individual existing housing not previously occupied, which is received on or after November 21, 1962, will not be assigned for appraisal prior to receipt of a certification from the builder, sponsor or other seller, in the form prescribed by the Secretary, that neither it nor anyone authorized to act for it will decline to sell any property included in such request to a prospective purchaser because of his or her race, color, religion, sex or national origin.

(b) On requests for appraisal of individual proposed construction received on or after November 21, 1962, the prescribed nondiscrimination certification will be required if the builder is to sell the veteran the lot on which the dwelling is to be constructed, but will not be required if:

(1) The veteran owns the lot; or

(2) The lot is being acquired by the veteran from a seller other than the builder and there is no identity of interest between the builder and the seller of the lot.

(c) Each builder, sponsor or other seller requesting approval of site and subdivision planning shall be required to furnish a certification, in the form prescribed by the Secretary, that neither it nor anyone authorized to act for it will decline to sell any property included in such request to a prospective purchaser because of his or her race, color, religion, sex or national origin. Site and subdivision analysis will not be commenced by the Department of Veterans Affairs prior to receipt of such certification.

(d) No commitment shall be issued and no loan shall be guaranteed or insured under 38 U.S.C. Chapter 37 unless the veteran certifies, in such form as the Secretary shall prescribe, that

(1) Neither he/she, nor anyone authorized to act for him/her, will refuse to sell or rent, after the making of a bona fide offer, or refuse to negotiate for the sale or rental of, or otherwise make unavailable or deny the dwelling or property covered by this loan to any person because of race, color, religion, sex, or national origin;

(2) He/she recognizes that any restrictive covenant on the property relating to race, color, religion, sex or national origin is illegal and void and any such covenant is specifically disclaimed; and

(3) He/she understands that civil action for preventive relief may be brought by the Attorney General of the United States in any appropriate U.S. District Court against any person responsible for a violation of the applicable law.

§36.4364 CORRECTION OF STRUCTURAL DEFECTS

(a) The purpose of this section is to specify the types of assistance that the Secretary may render pursuant to 38 U.S.C. 3727 to an eligible borrower who has been unable to secure satisfactory correction of structural defects in a dwelling encumbered by a mortgage securing a guaranteed, insured or direct loan, and the terms and conditions under which such assistance will be rendered.

(b) A written application for assistance in the correction of structural defects shall be filed by a borrower under a guaranteed, insured or direct loan with the Director of the Department of Veterans Affairs office having loan jurisdiction over the area in which the dwelling is located. The application must be filed not later than 4 years after the date on

which the first direct, guaranteed or insured mortgage loan on the dwelling was made, guaranteed or insured by the Secretary. A borrower under a direct, guaranteed or insured mortgage loan on the same dwelling which was made, guaranteed or insured subsequent to the first such loan shall be entitled to file an application if it is filed within 4 years of the date on which such first loan was made, guaranteed or insured by the Secretary.

(c) An applicant for assistance under this section must establish that:

(1) The applicant is the owner of a one- to four-family dwelling which was inspected during construction by the Department of Veterans Affairs or the Federal Housing Administration.

(2) The applicant is an original veteran-borrower on an outstanding guaranteed, insured or direct loan secured by a mortgage on such dwelling which was made, guaranteed or insured on or after May 8, 1968. The Secretary may, however, recognize an applicant who is not the original veteran-borrower but who contracted to assume such borrower's personal obligation thereunder, if the Secretary determines that such recognition would be in the best interests of the Government in the particular case.

(3) There exists in such dwelling structural defect, not the result of fire, earthquake, flood, windstorm, or waste, which seriously affects the livability of the dwelling.

(4) The applicant has made reasonable efforts to obtain correction of such structural defect by the builder, seller, or other person or firm responsible for the construction of the dwelling.

(d) In those instances in which the Secretary determines that assistance under this section is appropriate and necessary the Secretary may take any of the following actions:

(1) Pay such amount as is reasonably necessary to correct the defect, or

(2) Pay the claim of the borrower for reimbursement of the borrower's expenses for correcting or obtaining correction of the defect, or

(3) Acquire title to the property upon terms acceptable to the borrower and the holder of the guaranteed or insured loan.

(e) To the extent of any expenditure made by the Secretary pursuant to paragraph (d) of this section the Secretary shall be subrogated to any legal rights the borrower or applicant described in paragraph (c)(2) of this section may have against the builder, seller, or other persons arising out of the structural defect or defects.

(f) The borrower shall not be entitled, as a matter of right, to receive the assistance in the correction of structural defects provided in this section. Any determination made by the Secretary in connection with a borrower's application for assistance shall be final and conclusive and shall not be subject to judicial or other review. Authority to act for the Secretary under this section is delegated to the Chief Benefits Director.

(g) For the purpose of this section the term "structural defects seriously affecting livability" shall in no event be deemed to include (1) defects of any nature in a dwelling in respect to which the applicant for assistance under this section was the builder or general contractor, or (2) structural features, improvements, amenities, or equipment which were not taken into account in the Secretary's determination of reasonable value.