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Loan Guaranty: Loan Servicing and Claims Procedures Modifications; Final Rule

DEPARTMENT OF VETERANS AFFAIRS

38 CFR Part 36

RIN 2900–AL65

Loan Guaranty: Loan Servicing and Claims Procedures Modifications

AGENCY: Department of Veterans Affairs.

ACTION: Final rule.

SUMMARY: This document establishes a new series for the Department of Veterans Affairs (VA) Loan Guaranty regulations, which will be phased in over an approximately eleven-month timeframe, as mortgage servicing industry segments ''go live'' on a new computer-based tracking system being established by VA. This new series replicates existing regulations for most aspects of the VA Loan Guaranty program, but also includes changes related to several aspects of the servicing and liquidating of guaranteed housing loans in default, and the submitting of guaranty claims by loan holders. Specific topics revised in the new 4800 series include: increasing authority of servicers to implement loss-mitigation options, making incentive payments to servicers for successful loss-mitigation options, establishing a system of measuring and ranking servicer performance, establishing updated reporting requirements, permitting loan holders to review liquidation appraisals, requiring holders to calculate the net value of the security property prior to foreclosure, establishing a timeframe for when foreclosure of a defaulted loan should be completed, limiting the amount of interest and other fees and charges that may be included in a guaranty claim, establishing allowable attorneys fees to be included in the guaranty claim, establishing a deadline for the submission of guaranty claims, modifying the requirements for title evidence for properties conveyed to VA following foreclosure, modifying the requirements for how long a holder must maintain records relating to loans for which VA has paid a claim on the guaranty, and eliminating the requirement for the submission of legal procedural papers to VA. This document also includes specific revisions to three rules related to increased attorney fee allowances, establishment of a time limit for filing a claim under the guaranty, and granting authority for the Servicer Appraisal Processing Program that will be effective for all program participants upon publication of these rules.

DATES: This rule is effective February 1, 2008.

FOR FURTHER INFORMATION CONTACT: Mike Frueh, Assistant Director for Loan Management (261), Veterans Benefits Administration, Department of Veterans Affairs, 810 Vermont Avenue, NW., Washington, DC 20420, at 202–461–9521. (This is not a toll-free telephone number.)

SUPPLEMENTARY INFORMATION:

Statutory Background

Under 38 U.S.C. chapter 37, VA guarantees loans made by private lenders to veterans for the purchase, construction, and refinancing of homes owned and occupied by veterans.

Business Process Reengineering Review

Beginning in 2001, VA conducted an internal, in-depth review of the entire Loan Administration process that was effectively a business process reengineering (BPR) effort. ''Loan Administration'' includes the servicing of existing loans, dealing with loans in default and loans being terminated, and the processing of claims by loan holders under the guaranty after defaulted loans have been foreclosed or otherwise terminated. Loan Administration also includes efforts by VA and private loan holders to assist homeowners whose loans are in default to cure the default, retain their home if possible, or find other means short of foreclosure. VA's BPR team recommended revising the Loan Administration process to reflect changes in the loan servicing industry in recent years, as well as advances in technology. VA's BPR team also recommended placing greater reliance on private sector servicing in accordance with VA guidelines, with VA using advanced technology to oversee servicing actions.

Regulatory Background

On February 18, 2005 (70 FR 8472), VA proposed to amend its loan guaranty regulations in order to implement the following recommendations proposed by the BPR team: giving servicers increased authority to implement loss-mitigation alternatives to foreclosure and paying servicers an incentive bonus for each successful loss-mitigation alternative to foreclosure; establishing a performance-based tier-ranking system for servicers; permitting qualified loan holders to review liquidation appraisals and establish the fair market value of the property; requiring loan holders to calculate the net value of properties securing loans prior to foreclosure; establishing timeframes for when VA would expect holders, exercising reasonable diligence, should be able to complete the foreclosure of defaulted loans; limiting the amount of interest and other fees and charges that may be included in a guaranty claim; establishing reasonable and customary attorney fees allowed to be claimed under the guaranty; establishing a deadline for holders to submit claims under the guaranty and to request reconsideration of denied claims; modifying the requirements for title evidence submitted to VA when the holder is conveying the property to VA following the liquidation sale; modifying the requirements for how long a holder must maintain records relating to loans for which VA has paid a claim on the guaranty; modifying the requirements for holders to report key events with regard to loans being serviced; and repealing the requirement for holders to provide VA with procedural papers in legal or equitable proceedings related to a loan on the security property. VA published a supplemental notice on November 27, 2006 (71 FR 68498), to provide specific information regarding the computer-based system that VA proposed to implement as part of the loan servicing and claims procedure modifications. VA published another supplemental notice on June 1, 2007 (72 FR 30505), to provide information on a decision to phase-in implementation of most of the new rules, based on previous comments from the industry and the development of VA's computer-based tracking system.

Discussion of Public Comments

The initial public comment period closed on April 19, 2005. VA received 51 comments from the public about various aspects of the proposed changes. The public comment period was reopened following publication of the first supplemental notice and closed December 11, 2006. VA received an additional 8 comments from the public about the proposed reporting requirements for VA's new computer-based system. The public comment period was again reopened following publication of the second supplemental notice and closed June 15, 2007. VA received 2 comments from the public about its proposed phased implementation and clarifications regarding modifications.

The final rule has been revised to incorporate changes that VA agrees are necessary in light of, or as the logical outgrowth of, the comments provided. In order to accommodate the phased implementation of the new rules, VA is establishing a new subpart F (§§ 36.4800 through 36.4893, inclusive) of part 36 that contains substantive rules identical to those in the current rules (§§ 36.4300 through 36.4393). In addition, we redesignate those current rules as subpart B of title 38, CFR. Subpart F will be effective upon publication of this notice only for the first segment of the mortgage servicing industry, as described in the second supplemental notice published June 1, 2007 (72 FR 30505). The table below is similar to the one in that notice, and provides the effective date for the first segment that will be affected by these rules, as well as an indication of the time periods during which we expect to make these rules applicable to all other segments of the industry (although these time periods may change due to unforeseen circumstances). We will publish as notices in the **Federal Register** the actual applicability dates for industry segments two through nine.

Segment No.	Applicability date of phased-in rules (by calendar year quarter)
1	February 1, 2008.
2	2nd Quarter, 2008.
3	2nd Quarter, 2008.
4	4th Quarter, 2008.
5	2nd Quarter, 2008.
6	3rd Quarter, 2008.
7	3rd Quarter, 2008.
8	3rd Quarter, 2008.
9	4th Quarter, 2008.

Subpart B will continue to be the governing rules for industry segments until the dates they become subject to the new subpart F. VA is aware that certain portions of subpart B, specifically §§ 36.4302 and 36.4312, are in need of revision to match recent legislative amendments, as well as to update VA positions on certain requirements. However, in order to avoid confusion with those issues not directly impacting the servicing and liquidating of guaranteed housing loans in default, and the submitting of guaranty claims by loan holders, those changes have not been included in this rulemaking. Instead, VA is preparing proposed changes to §§ 36.4302 and 36.4312 in subpart B and in the corresponding §§ 36.4802 and 36.4813 in the new subpart F, and will request comments from the public on those changes after the effective date of these new rules.

In our review of subpart B, we also identified a number of minor errors, such as erroneous cross-references, typographical errors, and hanging provisions (flush text) that needed reformatting, and have corrected these wherever necessary in the new subpart F. However such corrections have not affected the rights, responsibilities, or obligations of program participants.

The following paragraphs discuss the comments VA received in response to the proposed rules and the supplemental notices. The paragraphs are in order by the new subpart F section number and provide VA responses. The preamble does not discuss sections about which we did not receive any public comment. The preamble also does not discuss any section that is substantively the same as its counterpart in §§ 36.4300 through 36.4393. However, such a section may contain conforming renumbering changes and/or technical revisions or reorganization. This final rule includes three changes to subpart B in §§ 36.4313(b)(5), 36.4321(d), and 36.4344a, and the comments and rationale for those changes are the same as those in the comments and responses on the new final rules in corresponding §§ 36.4814(b)(5), 36.4824(d), and 36.4848.

36.4800 Applicability of §§ 36.4800 Through 36.4893, Inclusive

Comment: VA should consider the time needed to adapt industry servicing systems and carefully test all aspects of the proposed electronic reporting requirements. This could also include special circumstances such as recent acquisitions, changes in servicing platforms, or other unforeseen situations.

VA Response: VA has carefully considered the factors that are essential to the success of its new electronic reporting environment, and determined that a phased implementation by industry segment offers the best chance for success. Accordingly, VA has established nine industry segments for program participants, with each segment ''going live'' on VA's new computer-based tracking system over an approximately 11-month timeframe. Each phase of implementation will include time for data clean-up, system modifications, defect corrections, testing of interfaces and data transmission, and review of lessons learned before initiating the next phase. Throughout this phase-in process, VA will remain flexible in adjusting its implementation schedule in order to accommodate participants' unique circumstances, such as changes in servicing platforms or unforeseen events. In addition, VA has the authority under § 36.4838 to administratively offer relief to entities not meeting VA requirements, such as electronic reporting.

36.4801 Definitions

Comments: VA should provide its definitions of ''repayment plans'' and ''special forbearances.''

VA Response: When VA published the proposed rule to replace the existing § 36.4317 with an arrangement to establish incentive payments for loss mitigation options, VA believed that the mortgage industry had a common understanding of the basic concepts of repayment plans and special forbearance agreements. However, while reviewing comments, and in researching definitions established by major industry participants (Fannie Mae, Freddie Mac, and the Department of Housing and Urban Development [HUD]), VA realized that each entity has its own slightly different definition for each of these terms. Accordingly, VA has added detailed definitions of ''repayment plan'' and ''special forbearance'' in this final rule in § 36.4801 to avoid any confusion as to what is required for each of these types of loss mitigation actions. VA is also clarifying the role of the servicer by adding a definition to state that the servicer is the entity which will be assigned a tier ranking based on its performance and will receive any incentive payment on a loan it services for the loan holder. The definitions are only minor clarifications of basic concepts customary in the loan servicing industry and do not impose any new requirements or take away any substantive rights of program participants. VA has listed all of the loss mitigation options in § 36.4819 in their preferred order of consideration (i.e., a hierarchy for review), but recognizes that individual circumstances may lead to ''out of the ordinary'' procedures. VA also plans to provide more detailed examples and advice on a number of issues, including repayment plans and special forbearances, as part of the training it will provide to servicers after publishing these rules.

Comment: VA should clarify the payment of incentives for successful loss mitigation efforts.

VA Response: VA concurs. The holder is the entity ultimately responsible for compliance with VA regulations and under § 36.4801 ''Holder'' includes ''the authorized servicing agent of the lender or assignee or transferee.'' However, for purposes of tier ranking (§ 36.4818) and loss mitigation options and incentives (§ 36.4819), VA's intent is to measure performance of the actual loan servicer and reward it accordingly. In order to make this distinction clearer, we provide a definition in § 36.4801 of ''servicer.'' The authorized servicer is either the servicing agent of a holder; or the holder itself, if the holder is performing all servicing functions on a loan. The servicer is typically the entity reporting all loan activity to VA and filing claims under the guaranty on behalf of the holder. VA will generally issue guaranty claims and other payments to the servicer, who will be responsible for forwarding funds to the holder in accordance with its servicing agreement. Incentives under § 36.4819 will generally be paid directly to the servicer based on its performance under that section and in accordance with its tier ranking under § 36.4818.

Comment: VA should clarify the procedures and implications of debt reductions used to ensure a property is eligible for conveyance to VA.

VA Response: In § 36.4823, we clarify the procedures to be followed to reduce debts in order to gain the right to convey to VA properties acquired at liquidation sales. However, to avoid confusion with multiple definitions of similar terms, we do not use the terms ''Indebtedness'', ''Specified amount'' and ''Unguaranteed portion of the indebtedness'' in this final rule in § 36.4801; that section will instead use the term ''Total indebtedness.'' The terms are defined in § 36.4301 because they are used primarily in §§ 36.4320 and 36.4321. However, the new final §§ 36.4823 and 36.4824 do not contain them and refer only to the total indebtedness as defined in the statute and the new final § 36.4801.

The other definitions included in § 36.4801 that are different from those in § 36.4301 were previously proposed.

36.4809 Transfer of Title by Borrower or Maturity by Demand or Acceleration

In § 36.4308(g), we refer to a time period specified in § 36.4316, which in turn establishes a three-month waiting period prior to the filing of a notice of intention to foreclose. The reporting and processing of defaults is handled differently under the new rules in §§ 36.4800 through 36.4893, and § 36.4818 does not refer to a waiting period. Therefore, in § 36.4809(g), we do not refer to another section but rather refer to the actual time frame of three months.

36.4814 Advances and Other Charges

Comment: VA should review its proposed foreclosure attorney fee schedule, which is very similar to those published by HUD, Fannie Mae, and Freddie Mac in 2001, to account for reasonable increases in living costs over the past several years, as well as other cost increases since that time due to increased labor and operational expenses for attorneys.

VA Response: VA concurs. VA has carefully reviewed the proposed foreclosure attorney fee schedule and has adjusted the amounts in accordance with the information provided in the comments, as well as updated information obtained from other sources. The table provided below, as referenced in final rules § 36.4313(b)(5)(ii) and § 36.4814(b)(5)(ii), is reasonably consistent with the fees allowed by other agencies for comparable work, and the commitment in paragraph (b)(5)(ii) to review the schedule annually will ensure the opportunity to timely address any imbalance in the schedule. In addition, VA has slightly modified the proposed language in new final rules § 36.4313(b)(5)(iii) and § 36.4814(b)(5)(iii) to allow additional trustee fees, above those allowed for legal services, when the trustee conducting the sale must be a Government official under local law, or if an individual other than the foreclosing attorney (or any employee of that attorney) is appointed as part of judicial proceedings, and local law also establishes the fees payable for the services of the public or judicially appointed trustee.

VA intends to reimburse only for attorney fees for services related to foreclosure of loans. Most of the attorneys commenting on the proposed rule reported that over the past five years many servicers have been outsourcing the foreclosure oversight process (i.e., hiring third parties to perform functions previously handled as part of the servicer's routine duties), and firms providing such outsourcing services are charging attorney firms a fee for providing the file needed to initiate the foreclosure action. While VA understands that servicers may find efficiencies in outsourcing certain functions, the cost for such outsourcing must be considered as an operating expense of the firm contracting for the outsourcing; i.e., the servicer. VA cannot consider outsourcing fees to be part of the cost of an attorney fee for completing a foreclosure. Consistent with our proposed rule, VA is establishing maximum amounts for legal services in each State, and those amounts are intended to reimburse for reasonable attorney fees. This is consistent with the position taken by Freddie Mac, which prohibits payment for referral fees, packaging or other similar fees, and new case start-up fees in its Single Family Seller/Servicer Guide, Volume 2, Chapter 71, section 71.18. Fannie Mae also notes in its 2006 Servicing Guide, Part VIII, Chapter 1, section 104.03, that it will not reimburse a servicer for legal fees and expenses related to actions that are essentially servicing functions.

Comment: VA should allow a fee to cover the costs of restarting a foreclosure that has been postponed, for example, by the filing of a bankruptcy petition. This would be in addition to the reimbursement for obtaining relief from the bankruptcy stay.

VA Response: VA concurs. VA recognizes that this is occurring more frequently, and is a true cost of doing business. Therefore, VA has allowed in the table provided herein in accordance with the final rules § 36.4313(b)(5)(ii) and § 36.4814(b)(5)(ii) an additional $350 ''foreclosure restart'' fee when a foreclosure sale is postponed or cancelled through no fault of the servicer or its foreclosure attorney. This includes but is not limited to bankruptcy, VA requested delay, property damage, hazardous conditions, condemnation, natural disaster, property seizure, or relief under the Servicemembers Civil Relief Act.

Comment: VA should consider increasing its maximum allowable bankruptcy fees, for reasons similar to those suggested for foreclosure fees.

VA Response: VA concurs. VA has reviewed the fees allowed by other entities, as well as the arguments made for increasing bankruptcy fees. VA believes that a modest adjustment is appropriate at this time and is revising the table referenced in the final rules in § 36.4313(b)(5)(ii) and § 36.4814(b)(5)(ii) to allow attorney fees of $650 (Chapter 7) or $850 (initial Chapter 13) for obtaining bankruptcy releases directly related to loan termination. For additional relief filed under either chapter, VA will allow an additional $250. VA will continue to monitor these fees on an annual basis.

The current legal services table is as follows:

Jurisdiction	Non-judicial foreclosure	Judicial foreclosure	Deed-in-lieu of foreclosure	Foreclosure restart fee [2]	Chapter 13 release [3]	Chapter 7 release [3]
Alabama	550	N/A	350	350	850	650
Alaska	1200	N/A	350	350	850	650

Jurisdiction	Non-judicial foreclosure	Judicial foreclosure	Deed-in-lieu of foreclosure	Foreclosure restart fee [2]	Chapter 13 release [3]	Chapter 7 release [3]
Arizona	625	N/A	350	350	850	650
Arkansas	750	N/A	350	350	850	650
California	600	N/A	350	350	850	650
Colorado	800	N/A	350	350	850	650
Connecticut	N/A	1250	350	350	850	650
Delaware	N/A	950	350	350	850	650
District of Columbia	600	N/A	350	350	850	650
Florida	N/A	1200	350	350	850	650
Georgia	600	N/A	350	350	850	650
Guam	1200	N/A	350	350	850	650
Hawaii	N/A	1850	350	350	850	650
Idaho	600	N/A	350	350	850	650
Illinois	N/A	1100	350	350	850	650
Indiana	N/A	1000	350	350	850	650
Iowa	550	850	350	350	850	650
Kansas	N/A	850	350	350	850	650
Kentucky	N/A	1100	350	350	850	650
Louisiana	N/A	900	350	350	850	650
Maine	N/A	1250	350	350	850	650
Maryland	800	N/A	350	350	850	650
Massachusetts	N/A	1250	350	350	850	650
Michigan	650	N/A	350	350	850	650
Minnesota	650	N/A	350	350	850	650
Mississippi	550	N/A	350	350	850	650
Missouri	650	N/A	350	350	850	650
Montana	600	N/A	350	350	850	650
Nebraska	600	850	350	350	850	650
Nevada	600	N/A	350	350	850	650
New Hampshire	900	N/A	350	350	850	650
New Jersey	N/A	1300	350	350	850	650
New Mexico	N/A	900	350	350	850	650
New York—Western Counties [1]	N/A	1250	350	350	850	650
New York—Eastern Counties	N/A	1800	350	350	850	650
North Carolina	550	N/A	350	350	850	650
North Dakota	N/A	900	350	350	850	650
Ohio	N/A	1100	350	350	850	650
Oklahoma	N/A	900	350	350	850	650
Oregon	675	N/A	350	350	850	650
Pennsylvania	N/A	1250	350	350	850	650
Puerto Rico	N/A	1100	350	350	850	650
Rhode Island	900	N/A	350	350	850	650
South Carolina	N/A	850	350	350	850	650
South Dakota	650	850	350	350	850	650
Tennessee	550	N/A	350	350	850	650
Texas	550	N/A	350	350	850	650
Utah	600	N/A	350	350	850	650
Vermont	N/A	950	350	350	850	650
Virginia	600	N/A	350	350	850	650
Virgin Islands	N/A	1100	350	350	850	650
Washington	675	N/A	350	350	850	650
West Virginia	550	N/A	350	350	850	650
Wisconsin	N/A	1100	350	350	850	650
Wyoming	600	N/A	350	350	850	650

[1] Western Counties of New York are: Allegany, Cattaraugus, Chautauqua, Erie, Genesee, Livingston, Monroe, Niagara, Ontario, Orleans, Steuben, Wayne, Wyoming, and Yates. The remaining counties are in Eastern New York.

[2] When a foreclosure is stopped due to circumstances beyond control of the holder or its attorney (including, but not limited to bankruptcy, VA-requested delay, property damage, hazardous conditions, condemnation, natural disaster, property seizure, or relief under the Servicemembers Civil Relief Act) and then restarted, VA will allow the restart fee in addition to the base foreclosure attorney fee.

[3] For each additional relief of stay under either chapter, VA will pay $250.

Comment: VA should publish a single national reimbursable fee schedule so that servicers will be able to accurately calculate total indebtedness. VA should provide at least 30 days advance notice of changes in fees to allow for system updates and procedural modifications.

VA Response: VA does not concur at this time because this information is maintained at the Regional Loan Center (RLC) level in order to be updated as quickly as possible when local changes occur, so that holders may be reimbursed for actual expenses as they occur, rather than experiencing a lag time. The current schedules provide the local fees and expenses and we believe that this data should continue to be provided at the local level. However, VA will initiate plans to post such a national schedule of fees when this can be accomplished in a timely manner.

36.4815 Loan Modifications

Comment: VA should not require holders to reduce the interest rate on a loan modification where market interest rates have decreased since the date of loan origination.

VA Response: VA does not concur, but is changing the new final rule in § 36.4815 in an effort to make it easier for servicers to administer. The existing VA regulation dealing with loan modifications (§ 36.4314) allows no change to the interest rate on the loan. In fact, another regulation (§ 36.4311(c)) specifically states that interest in excess of the rate reported by the lender when requesting evidence of guaranty shall not be payable. The vast majority of VA-guaranteed loans are securitized in GNMA (Government National Mortgage Association) insured pools, which require the holder to purchase the loan from the pool in order to modify the loan. The proposed change recognized the difficulty faced by loan servicers in attempting to resecuritize loans with interest rates well below the market average, and thus allowed for increasing interest rates on modifications when market conditions dictate. However, VA also believes it is only fair to veterans to similarly reduce interest rates when market rates have decreased since loan origination. The impact of reduced interest rates would be similar to the effect of other creditworthy borrowers refinancing at lower interest rates, and should not adversely affect VA lenders. Therefore, VA is not departing from requiring an interest rate reduction where market interest rates have decreased since loan origination. VA is, however, removing the one percent cap on interest rate increases that had been contained in the proposed rule so that modifications will become a more widely used tool to help veterans retain their homes. VA is also slightly modifying the language that had been in paragraph (c) of the proposed rule in § 36.4314 to make adjustments easier, by allowing the maximum interest rate to be based on a month-end rate, rather than requiring a daily adjustment as the proposed rule had provided. Therefore, § 36.4812(c) is changed to allow a higher interest rate on a modified loan. The final rule in § 36.4815 is changed as described above to remove the one percent cap on increases and to clarify the date to be used in establishing the new maximum interest rate allowable on a modified loan.

Comment: VA should increase the guaranty on a modified loan to match the percentage guaranteed at loan origination, rather than only allowing an increase in the amount of guaranty if it would otherwise provide less than 25% guaranty of the modified loan amount.

VA Response: VA does not concur. The proposal in § 36.4314(g) to increase the guaranty on a modified loan to 25% of the loan amount was another effort to help modified VA-guaranteed loans qualify for resecuritization. Under the existing § 36.4314, the amount of the guaranty does not increase upon loan modification, which means that the percentage of guaranty, in effect, will decrease if the modified loan amount is greater than the original loan amount. This is important because all VA-guaranteed loans greater than $144,000 at origination have a maximum 25% guaranty, and the average new loan is often well above that amount. Under the existing § 36.4314 any such loan being modified would retain the same amount of guaranty, and thus have an effective percentage of guaranty less than 25% whenever the modified loan amount is greater than the original loan amount. This final rule in § 36.4815(h) (due to minor realignment of the section paragraphs) allows the guaranty amount on the modified loan to increase up to 25% of the modified loan amount, subject to the maximum amount of guaranty allowable under the law. This should be sufficient to allow repooling in a new GNMA-insured security, and provide adequate risk sharing for the modified loan among VA, the holder, and GNMA. Therefore, no further revision is necessary, other than conforming language in §§ 36.4802(h) and 36.4824(a).

Comment: VA should not require the same underwriting standards for loan modifications as those used at loan origination.

VA Response: VA does not concur. VA's existing § 36.4314(a) governing loan modifications requires that the holder determine that the borrower is a satisfactory credit risk, and the proposed rule did the same by referencing the criteria in § 36.4337. In establishing that the veteran is a satisfactory credit risk, there must be an analysis of the veteran's income and obligations, as well as a review of the credit history. The proposed rule specifically addressed the issue of credit history with respect to the event(s) that led to the need for loan modification, and the criteria in § 36.4337 provide for the acknowledgement of compensating factors to address issues that might otherwise preclude the extension of credit. VA therefore believes the proposed regulation was sufficiently flexible to accommodate the assessment of the creditworthiness of borrowers who seek to modify their loans, and no changes are necessary in the final § 36.4815(a). A specific comment requested that the use of ''in-file'' credit reports be allowed to reduce costs, and VA agrees this will be in accordance with the way its underwriting criteria have been interpreted in order to expedite processing.

Comment: VA should make provision for other expenses of modification not being rolled into the new loan.

VA Response: VA concurs. The existing § 36.4314 makes no provision for inclusion of any expenses in the modified loan amount. The proposed rule provided that only certain items could be included in the modified indebtedness. VA carefully reviewed the comments on this subject and is clarifying § 36.4815(e) so that it addresses all possible expenses of modification. In addition to allowing holders to include unpaid principal, accrued interest, and deficits in the taxes and insurance impound accounts in the modified indebtedness, holders will also be allowed to capitalize advances required to preserve their lien position, such as homeowner association fees, special assessments, water and sewer liens, etc. By limiting the items that may be included in the modified loan indebtedness, VA is attempting to protect both the interests of the Government and the veteran borrower by keeping the potential loan-to-value (LTV) ratio as low as possible, while recognizing that it may often exceed 100%. In a case where modification is determined to be the best alternative early in the course of a default, there will be little else in the way of other fees and expenses that need to be paid. In such a case the borrower should be able to handle those other costs as a demonstration of creditworthiness, and after including the expenses allowed by the new final rule in the modified loan amount, the resulting LTV ratio may not be significantly different than at loan origination. If a default has continued for quite some time before modification is deemed feasible, then it is likely that the additional fees and costs may have accrued to a sum equal to one or more monthly mortgage payments. VA never envisioned that such fees and costs would be forgiven by the loan holder. Because the modification process involves some period when regular payments are not made on the loan, the borrower should be able to accumulate funds to cover the fees and costs accrued during the default, rather than having them rolled into the modified loan indebtedness. This is similar to the HUD requirements for modifications. As for any costs associated with processing the modification, VA expects that the incentives paid for successful modifications will offset such expenses, and VA will not allow any processing costs to be charged to the borrower as stated in the final § 36.4815(f).

Comment: VA should not require that all current owners occupy the property and should pay for a title insurance policy covering the modified loan.

VA Response: VA agrees that occupancy should not be a requirement because the basic program requirements do not require continued occupancy in order for the guaranty to remain in effect (i.e., at some point a veteran borrower may move from the home securing the VA-guaranteed loan, but that does not invalidate the guaranty). Hence, § 36.4815(a) will not require that all current owners occupy the property.

As for title insurance policies, existing VA regulation § 36.4828(b) does require that holders obtain and retain a lien of proper dignity against the security property, and title insurance is often used at loan origination to satisfy this requirement. If a holder decides to require title insurance in connection with a loan modification to ensure its lien status, then VA would not object to a reasonable expense to the buyer for this service. Since in most cases a title insurance policy was obtained at loan origination, any insurance obtained at modification would only need to cover the period from loan origination to the date of modification, and it is expected that the cost for a title endorsement, or other form of insurance ''update,'' would be considerably less than the amount paid at loan origination. The final rule in § 36.4815(f) slightly revises the proposed rule to provide this clarification.

Comment: VA should not require that all current owners agree to the modification.

VA Response: VA does not concur. VA is retaining the provision in the new final rule in § 36.4815(a)(5) that all current owners must be obligated on the loan and participate in any modification, because it would not be fair to allow a change in the terms of a loan secured by a property without first notifying all parties with an ownership interest in that property and obtaining their agreement to the change. If a holder encounters unusual circumstances that lead it to believe a modification not meeting the requirements in § 36.4815(a)(1)–(6) would be beneficial to a veteran, then the case may be submitted to VA for prior approval.

Comment: VA should not restrict the number of times that a loan may be modified because other agencies/investors have no such limits.

VA Response: Under § 36.4314, we permit three modifications to any one loan without prior VA approval, but also may allow unlimited modifications with prior VA approval. To that extent, we agree with the comment.

However, to the extent that the comment requests unlimited modifications without VA review, VA does not concur because VA has a responsibility to ensure that loan modifications are fair to the borrower, and to protect the interests of the Government. The final rule in § 36.4815 provides sufficient flexibility to address almost all situations that may arise. Although the rule cannot address every possible circumstance, it does adequately provide for loss mitigation by authorizing holders in advance to modify the vast majority of loans, while allowing holders to seek direct approval from VA for unusual cases that do not fit the general criteria described in the regulation.

In order to avoid any misunderstandings about the authorizations granted, the final rule is modified by adding paragraph (j), which advises that the authority contained in § 36.4815 does not create a right of a borrower to have a loan modified but simply authorizes the loan holder to modify a loan in certain situations without the prior approval of the Secretary. This is in keeping with past VA policy and court decisions over the years that have found that VA's refunding program (§ 36.4820) is not a veteran's benefit, but rather an administrative option established by the regulation to enable VA to assist a veteran when VA makes the determination that the option is appropriate.

Comment: VA should include the words ''or default is imminent'' in § 36.4815(a)(1).

VA Response: VA does not concur. The proposed rule in § 36.4314(a) included those words and the second supplemental notice proposed deleting them. As stated in the second supplemental notice, because VA is proposing a hierarchy of loss mitigation options for consideration within the new regulatory package, it would not be appropriate for a holder to consider modification of a loan until after first considering a repayment plan or a period of forbearance in order to allow loan reinstatement. Therefore, it would not normally be feasible for a holder to consider modification of a loan where default is only imminent, because that would not allow for prior consideration of a repayment plan or a period of forbearance. However, if an unusual circumstance arises, a holder may seek direct approval from VA for approval of a case that does not fit the general criteria. Therefore, the final rule in § 36.4815(a)(1) will remain as proposed in the second supplemental notice.

36.4817 Servicer Reporting Requirements

Comment: VA should review its need for the requested data, should reduce the number of reportable items, and should eliminate the expedited, event-specific reporting.

VA Response: VA concurs for the most part. VA has carefully reviewed the report timing and the required items in the proposed rule in § 36.4315a in light of industry comments, consultation with information technology specialists, and review of the goals and operating procedures in VA's new loan servicing environment, as well as the reporting requirements of HUD, Fannie Mae, and Freddie Mac. In conducting this review, VA identified and retained only those items for reporting that VA determined absolutely necessary to conduct proper oversight of servicer actions. That oversight must include review of servicer actions that are being newly delegated by VA, servicer actions that were previously reviewed by VA utilizing extensive paper reports provided by servicers, and servicer actions that in the past were reviewed only upon submission of various documentation from servicers. Providing this information electronically should greatly reduce the time required for interaction between VA and servicers via telephone and written communications that occurs under the present operating procedures. VA has determined that a number of items (including escrow disbursements and legal actions other than terminations) will not be included in the list of what must be reported to VA. We discuss these items later in this document, responding to specific comments. In addition, remaining items for loans not in default may all be reported on a monthly basis (i.e., no later than the seventh calendar day of the month following the month in which the event occurred), while most of the items related to loan defaults will also be required on a monthly basis, rather than within five business days of an event. VA is changing these events and most of the remaining events that must be reported expeditiously to require reporting within 7 calendar days, rather than 5 business days because most tracking systems are not equipped to calculate business days, but can easily handle computation of calendar days.

As suggested by the comments, one item previously proposed to be reported on all loans, bankruptcy filing information, will only be required on loans reported in default. Only events denoting significant action on loans reported in default (such as referral to an attorney to initiate foreclosure, establishment of a liquidation sale date, advice that a sale has been held, etc.) will still need to be reported within seven calendar days of the event. As in the past, holders will need to notify VA within 15 calendar days of a liquidation sale when they desire to convey a property to VA.

An example of one item that was in the proposed rule § 36.4315a(c)(2) with a five business day reporting requirement was information on assumption of a VA-guaranteed loan. Existing rule § 36.4303 presently requires reporting of information on approved assumptions and unauthorized transfers of ownership. The first supplemental notice, which provided more detail on the specific events to be reported, required electronic reporting of transfer of ownership (i.e., an authorized assumption) and unauthorized transfer of ownership. In light of the comments, VA is not, under § 36.4817(c), requiring electronic reporting of unauthorized transfer of ownership, but is requiring electronic reporting of authorized transfer of ownership, which will be renamed accordingly. The final rule in § 36.4803(l)(2) continues to require the holder to notify VA within 60 days of learning of an unauthorized transfer, as in the existing § 36.4303(l)(2).

Comment: Information on the Servicemembers Civil Relief Act should only be required if that is a reason for delay of a foreclosure sale.

VA Response: VA concurs with deleting the requirement to report this event. If the event causes delay in loan termination, then information about it may be reported as part of the claim event reporting.

Comment: VA should allow reporting of multiple events occurring on a single loan during a monthly reporting period.

VA Response: VA agrees with this comment and the file reporting format will allow for multiple events to be reported on each loan.

Comment: The requirement to report substantial equity (25% or more) will necessitate a special title search and should be deleted, as it could require servicers to upgrade their systems to load junior lien information and to calculate the equity.

VA Response: VA concurs with deleting this requirement. VA proposed this requirement in § 36.4315a(f) in order to ensure review of cases where substantial equity could exist. However, after reviewing the other data requested and the computing capabilities offered by its new computer system, VA decided it can instead use the other reported data to calculate its own estimate of equity and take appropriate action to ensure that veterans receive every reasonable opportunity to salvage that equity prior to loss through foreclosure. Therefore, there is no requirement in the final rule to calculate or report substantial equity.

Comment: VA should consider using the HUD Single Family Default Monitoring System (SFDMS) file layout for reporting information, rather than requesting data that may not presently be available in many loan servicing systems.

VA Response: VA considered this possibility, but decided it was not feasible. As VA began developing the computer system that it will use to receive data from servicers, VA obtained considerable information about HUD's file layout and other systems from a leading provider of loan accounting and default tracking services, which is subcontracted to the contractor developing VA's system. As that development continued, it was clear that the information VA needs to monitor servicer activities that have been delegated will require more details than those obtained by HUD's SFDMS. This is due to different processes used by the agencies in conducting oversight, as well as making payments for incentives, acquisitions, and claims. VA has found that almost all of the data fields it is still seeking presently exist in most servicing systems. VA worked collaboratively with the providers of the most widely utilized loan servicing systems, and continued to reduce its data requirements as much as possible, in order to develop the easiest file layout and method of transmission for reporting. That layout has been posted on VA's public Web site. Therefore, VA expects that the industry will be able to easily comply with its remaining reporting requirements in § 36.4817.

Comment: VA should consider the potential cost to servicers of the additional reporting requirements, the time needed to implement those changes, and the security risks of transmitting additional information.

VA Response: VA has carefully considered all of those issues in developing its final reporting rule in § 36.4817.

VA recognizes that few changes can be made without some costs. However, by using a fixed width flat file layout, VA is utilizing the simplest format currently available for reporting data. Moreover, VA has developed a methodology to reduce the amount of computations required by most loan servicing platforms when extracting data from their systems to report events to VA. This should also significantly reduce the cost of changes. There will be a few additional data fields that most servicing systems will need to add over time, and VA realizes that there will be some expenses to accomplish this, but the result will be data that is available electronically rather than manually.

While there may be some programming costs incurred by servicers due to the additional reporting requirements in § 36.4817, VA expects that servicers will benefit in a number of ways. First, with the change to electronic reporting, servicers will greatly reduce their monthly expenses of reporting defaults and loan status updates via paper forms to VA, as well as reducing the time required by their employees to respond to written and telephone inquiries from VA. Second, the additional data required is for purposes of VA oversight, but that data should be of considerable value to servicers in tracking their internal servicing performance (for example, providing greater control over insoluble defaults and ensuring faster referral for termination, allowing closer review of payment plans to monitor performance, etc.). Third, having the data available electronically should eliminate many manual processes that are much more costly. VA expects there will be many more areas in which servicers will benefit from the availability of this new data.

VA is well aware that considerable lead time is needed in order to change loan servicing systems to capture additional data. VA has worked with its contractor and subcontractor to develop a phased approach to implementation of its new, computer-based tracking system, the VA Loan Electronic Reporting Interface (VALERI). VA will implement VALERI over an approximately 11-month timeframe, with program participants grouped into nine segments that will ''go live'' on VA's new system during designated phases of implementation. Each phase of implementation will incorporate time for data clean-up, system modifications, defect corrections, testing of interfaces and data transmission, and review of lessons learned before initiating the next phase. VA is also developing a Web portal to allow manual input of information that is not yet contained in major loan servicing systems, and for smaller servicers who may not utilize servicing system providers, although the ultimate goal is automated file transfers of all information.

Data security is of the utmost importance to VA. Servicer suggestions to delete requests for sensitive information, such as Social Security

Numbers (SSNs), have been honored as much as possible. VA will not request SSNs as part of the basic monthly reporting as originally proposed. Instead, the only request for SSNs will be when servicers report them for new loan assumers. Those SSNs and all other data will be encrypted during transmission, appropriate protocols will be established with each servicer and its loan servicing system (or provider) to ensure secure transmissions, and access to the data at VA and its contractors will be limited to authorized users.

36.4818 Servicer Tier Rankings—Temporary Procedures

Comment: In developing its tier rankings, VA should consider a methodology that is publicly disseminated and can easily be determined by servicers based on information available to them. VA should also incorporate some allowance for the purchase of delinquent loans from other servicers.

VA Response: VA concurs to an extent. In our development of a proposed rule to implement the tier ranking system, we will consider the negative impact of the purchase of delinquent loans from other servicers. In the preamble to this proposed rule, VA indicated an intent to model its tier ranking system after that used by the Federal Home Loan Mortgage Corporation (FHLMC), also known as Freddie Mac. After VA has collected data under its new reporting requirements for six months, VA intends to review the data and develop the criteria for ranking servicers. Those criteria will then be published in the **Federal Register** for notice and comment. Whether the final rule that implements the tier ranking system is similar to the Freddie Mac model will depend upon the data we collect and the comments we receive. VA expects that the computer system for collecting data will be operational in 2008, and proposed rules for tier ranking will be published in calendar year 2009. Accordingly, the final rule in § 36.4818 remains as proposed.

Comment: VA should consider paying incentives at higher than the Tier II ranking during the first year, either due to some assessment of higher performance, or else based on a servicer's participation in VA's current Server Loss Mitigation Program (SLMP).

VA Response: VA does not concur. The proposed rule § 36.4316(a) provided for four levels of tier rankings of servicers, with all servicers in Tier II for the initial ranking period as of the effective date of this rule. Because VA will have no published methodology for rating servicer performance during the first year of the new program, it would not be fair to attempt to determine which servicers should be paid at the Tier I or any other level, other than the initial Tier II rating for all servicers. While VA has had the SLMP in operation for many years, that program has not attempted to measure specific performance in a manner similar to the proposed Servicer Tier Ranking system, and the SLMP has only allowed two loss mitigation alternatives, and not the three home retention alternatives in the new program. Accordingly, it would not be fair to grant SLMP participants a higher tier ranking until the criteria for performance have been established. In any event, the proposed incentive payments for Tier II compare favorably to what VA allowed under SLMP, and have been adjusted slightly to account for the time elapsed since the initial publication of the proposed amounts, as well as changes by other agencies during that time. Therefore, the final rule in § 36.4818 remains as proposed.

36.4819 Servicer Loss Mitigation Options and Incentives

Comment: VA should simply adopt HUD (Department of Housing and Urban Development) loss mitigation procedures, fees, and reimbursement schedules, including incentive payment upon execution of a repayment plan, rather than waiting for final or partial completion of the plan to pay for the additional work required in analyzing data and establishing a plan.

VA Response: VA does not concur. VA carefully considered loss mitigation programs developed by HUD, Fannie Mae, Freddie Mac, and private mortgage insurers as part of its BPR project. Although most had attractive features, no one program by itself addressed all the issues of loss mitigation in the manner VA felt was necessary to ensure proper assistance to veterans, while also rewarding loan servicers in an appropriate fashion for success in mitigating potential losses.

As for the comment suggesting that incentives be paid upon execution of a repayment plan or special forbearance agreement because of the work involved in developing the plan, VA believes this is part of the normal activity of servicing a delinquent loan in order to determine whether it may be reinstated or whether the default is insoluble. While one comment was that loss mitigation efforts have historically been considered extraordinary servicing activity, VA believes that any servicer interested in properly managing its portfolio (and ensuring future servicing income) will exert reasonable efforts to obtain borrower financial information to determine the likelihood of loan reinstatement. Therefore, the incentives authorized under this section are in recognition of basic concepts customary in the loan servicing industry, and do not impose any new requirements or take away any substantive rights of program participants. However, paying an incentive simply for executing a repayment or forbearance agreement would not serve as a true incentive for developing a plan that is likely to succeed, but could instead encourage plans where success is improbable. Therefore, VA will not revise its program to make an incentive payable upon execution of a loss-mitigation alternative and the new final rules in §§ 36.4819 and 36.4822(e) and (f) (adjusted from (f) and (g)) remain generally as proposed. In order to clarify VA's intended use of the options and alternatives, they are listed in § 36.4819(b) from top to bottom in their preferred order of consideration (i.e., a hierarchy for review), but VA recognizes that individual circumstances may occasionally lead to ''out of the ordinary'' considerations.

Comment: VA should provide a partial claim loss mitigation benefit similar to that offered by HUD.

VA Response: VA does not concur. Under the HUD Partial Claim option, a mortgagee will advance funds on behalf of a mortgagor in an amount necessary to reinstate a delinquent loan (not to exceed the equivalent of 12 months PITI). The mortgagor will execute a promissory note and subordinate mortgage payable to HUD. Currently, these promissory or ''Partial Claim'' notes assess no interest and are not due and payable until the mortgagor either pays off the first mortgage or no longer owns the property.

The issue of a similar VA partial claim program has been discussed for many years within Congress and at VA. However, Congress has not specifically authorized VA to develop such a program. As explained above, partial claim payments are actually payments on behalf of homeowners to their loan holders, but VA has no authorization to make direct loans to borrowers to cover their delinquent payments, so a partial claim program is not feasible. Instead, VA believes that by encouraging holders to consider extended repayment plans or even loan modifications, borrowers should receive the assistance necessary to retain ownership of their homes. Therefore, VA does not concur that a partial claim program should be instituted in the new final rule in § 36.4819.

36.4820 Refunding of Loans in Default

Comment: VA should establish a process to extend the deadline to allow for recording of documents.

VA Response: VA does not concur. VA proposed in § 36.4318(c) to establish a deadline for submission of title documents on refunded loans, and to allow VA to impose a penalty for continued failure to comply with that deadline. VA must retain the option to take appropriate action when a holder has demonstrated a continued pattern of non-compliance with VA requests for timely delivery of documents that should be readily available, given the routine nature of loan transfers within the industry. VA has slightly modified the language to clarify that in accordance with the general rule, as applied throughout VA's regulations, notice to VA is deemed to be effective as of the date that VA receives such notice; notice from VA to others is deemed effective as of the date that VA sends or transmits such notice. If a holder encounters an occasional delay due to failure by a former servicer to adequately document a servicing transfer, for example, then VA does not expect to take the action authorized by the proposed rule in § 36.4318(c). On the other hand, if a servicer routinely fails to properly perform its duties on behalf of the holder and consistently fails to timely provide documents that should be readily available, and if the servicer fails to correct its practices after VA provides notice, then the final rule in § 36.4820(c) enables VA to focus the attention of the servicer to its problems by temporarily withholding all payments until the specific deficiencies cited by VA have been resolved. Therefore, the ''process'' proposed by the comment is not necessary and the final rule in § 36.4820 remains as proposed.

Comment: VA should make the title document requirements for refunding conform to the liquidation title package requirements.

VA Response: VA does not concur. The proposed rule § 36.4318 required provision of all legal documents required to evidence proper loan transfer. Refunding of a loan is simply an assignment, rather than a liquidation, and therefore does not involve documents establishing ownership of a property. Accordingly, the title document requirements for refunding review and conveyance of properties must be different. The final rule § 36.4820(c) remains as proposed.

36.4821 Service of Process

Comment: VA should define ''procedural papers'' in more detail—for example, does this include pleadings, claim back up, etc.?

VA Response: VA does not concur. The existing rule § 36.4319(a) requires that all ''procedural papers'' be provided to VA whenever a loan holder institutes suit or otherwise becomes a party in any legal or equitable proceeding brought on or in connection with the guaranteed or insured loan indebtedness, or involving title to, or other lien on, the security. The final rule § 36.4821(a) requires only that VA and the United States Attorney be provided with process when the Secretary of Veterans Affairs is actually named as a party to a legal action, which is effectively the definition of ''procedural papers'' that must be delivered to VA. VA has no specific requirement for the retention of pleadings or other actions in the normal course of a loan termination, although the final rule in § 36.4833 requires the holder to maintain a record of the amounts received on the obligation and disbursements chargeable thereto and the dates thereof, including copies of bills and receipts for such disbursements. This is the type of ''claim backup'' referenced in § 36.4824(d)(5), which provides that supporting documents will not be submitted with the claim under guaranty, but are subject to inspection as provided in § 36.4833. The final rule § 36.4821 remains as proposed.

36.4822 Loan Termination

Comment: VA should adjust the timeframes for foreclosure and also establish automatic extensions for many different types of delays.

VA Response: VA has reviewed all of the individual State timeframes for foreclosure in the proposed rule § 36.4319a(a), has taken into consideration the specific information provided in the comments on the processes, and is adjusting the timeframes in the final rule. In addition, VA is slightly revising the final § 36.4814(f)(2) and § 36.4824(a)(3)(ii), which describe the calculation of the maximum interest payable on a foreclosure, so that the calculation of the date to which interest will be paid shall include 210 calendar days from the due date of the last paid installment, in addition to the State calendar day timeframe for foreclosure. This is in response to comments requesting additional time for loss mitigation efforts. It equates to the present guideline used by VA in establishing interest cutoffs, in that it allows 180 days from the date of last paid installment (which is typically the time that VA requests initiation to terminate a loan), plus 30 days (which reflects the time allowed for initiation of such action under the existing § 36.4319(f)), plus the actual time to complete foreclosure. The timeframes will be reviewed as appropriate and changes published in the **Federal Register**, and maintained throughout the year on a Web site under VA's control, such as at *http://www.homeloans.va.gov.* The timeframes have been revised to reflect that the timeframes are in calendar days. The timeframes effective as of the date of this rule are as follows:

Jurisdiction	Procedure	Final event	Time frame (calendar days)
Alabama	Non-Judicial	Sale	60
Alaska	Non-Judicial	Sale	120
Arizona	Non-Judicial	Sale	120
Arkansas	Non-Judicial	Sale	90
California	Non-Judicial	Sale	150
Colorado	Non-Judicial	Sale	150
Connecticut	Judicial	Sale (Vesting Date)	180
Delaware	Judicial	Confirmation/Ratification	240
District of Columbia	Non-Judicial	Sale	60
Florida	Judicial	Confirmation/Ratification	150
Georgia	Non-Judicial	Sale	90
Guam	Non-Judicial	Sale	180
Hawaii	Judicial	Confirmation	240
Idaho	Non-Judicial	Sale	180

Jurisdiction	Procedure	Final event	Time frame (calendar days)
Illinois	Judicial	Sale	300
Indiana	Judicial	Sale	270
Iowa	Judicial	Sale	180
	Non-Judicial	Sale (Filing of Affidavit)	60
Kansas	Judicial	Sale	150
Kentucky	Judicial	Confirmation	150
Louisiana	Judicial	Sale	180
Maine	Judicial	Sale	300
Maryland	Non-Judicial	Ratification Date	90
Massachusetts	Judicial Order	Sale	180
Michigan	Non-Judicial	Sale	90
Minnesota	Non-Judicial	Sale	90
Mississippi	Non-Judicial	Sale	90
Missouri	Non-Judicial	Sale	60
Montana	Non-Judicial	Sale	150
Nebraska	Judicial	Confirmation	180
	Non-Judicial	Sale	120
Nevada	Non-Judicial	Sale	150
New Hampshire	Non-Judicial	Sale	90
New Jersey	Judicial	Sale	300
New Mexico	Judicial	Confirmation	180
New York—Western Counties [1]	Judicial	Sale	240
New York—Eastern Counties	Judicial	Sale	270
North Carolina	Non-Judicial	Sale	120
North Dakota	Judicial	Sale	240
Ohio	Judicial	Confirmation	360
Oklahoma	Judicial	Confirmation	210
Oregon	Non-Judicial	Sale	150
Pennsylvania	Judicial	Sale	270
Puerto Rico	Judicial	Confirmation	450
Rhode Island	Non-Judicial	Sale	90
South Carolina	Judicial	Sale	180
South Dakota	Judicial	Sale	150
	Non-Judicial	Sale	90
Tennessee	Non-Judicial	Sale	60
Texas	Non-Judicial	Sale	90
Utah	Non-Judicial	Sale	150
Vermont	Judicial	Sale	300
Virginia	Non-Judicial	Sale	60
Virgin Islands	Judicial	Sale	540
Washington	Non-Judicial	Sale	150
West Virginia	Non-Judicial	Sale	60
Wisconsin	Judicial—Abandoned	Confirmation	210
	Judicial—Tenant Occupied	Confirmation	240
	Judicial—Owner Occupied	Confirmation	330
Wyoming	Non-Judicial	Sale	90

[1] Western Counties of New York are: Allegany, Cattaraugus, Chautauqua, Erie, Genesee, Livingston, Monroe, Niagara, Ontario, Orleans, Steuben, Wayne, Wyoming, and Yates. The remaining counties are in Eastern New York.

As for automatic extensions of timeframes due to delays beyond the control of the holder, VA has been developing its system to accomplish this, based on event updates provided by holders. In determining those events that are beyond the control of the holder, VA considered the policy of HUD and the other comments provided. VA believes the largest factor causing delays in foreclosures is the filing of bankruptcy petitions, and by receiving information on such actions as part of the normal event reporting, VA will have on hand the information to automatically adjust the interest computation date when calculating the claim payable under § 36.4824.

When VA receives notice of a bankruptcy filing, the system should automatically allow up to 180 calendar days to enable the servicer to obtain relief from the bankruptcy. VA believes this should be sufficient for most single filings and may cover some multiple bankruptcy cases. If more time is needed, the servicer can request approval from VA for additional time due to delays caused by multiple bankruptcy filings.

VA believes that many of the other events mentioned in the comments as beyond the control of the holder are very infrequent and do not require a process to automatically account for those delays in claim calculation. First, this final rule provides VA the discretion to treat such delays as exceptions and then to allow the holder to justify charging additional interest if the delays extend completion of the liquidation past the timeframe calculated under § 36.4824(a)(3). Given this discretionary authority, we do not find it necessary to incorporate specific rules as to infrequent events. Furthermore, VA does not believe that additional interest should be payable for delays that are generally within the control of the loan holder, such as title issues or missing documents that the holder should have resolved in the normal course of business, rather than waiting until termination to seek resolution. However, we recognize that some delays may require detailed review and exchange of information to establish whether they were beyond the control of the holder. VA's regulations are flexible enough to allow for this.

Comment: VA should eliminate the requirement for a promissory note in connection with deeds-in-lieu of foreclosure and compromise sales.

VA Response: VA concurs. VA reviewed the proposed rule, § 36.4319a(f)(v), (g)(vi), and (h), which required a promissory note in connection with certain deeds-in-lieu of foreclosure and compromise sales, as well as the comments concerning the additional work required in calculating whether a promissory note would be required, and the work necessary to actually obtain such a note. Because the purpose in authorizing deeds and compromise sales is to expedite the processing of such alternatives, and because VA has the authority in § 36.4826(e)(1) to approve a complete release of the Secretary's right to collect a debt related to payment of a claim under the loan guaranty, and the law governing the program provides in 38 U.S.C. 3703(e) that the majority of veterans will not be liable for such indebtedness following loan default, VA has decided to automatically determine that the cooperation of the borrower in completing a deed-in-lieu of foreclosure or a compromise sale is sufficient to justify VA waiver of collection of any indebtedness. Accordingly, the final version of § 36.4822 does not require the holder to obtain a promissory note in connection with a deed-in-lieu of foreclosure or a compromise sale.

VA has also removed the requirements proposed in §§ 36.4319a(f)(iii) and 36.4319a(g)(iv) that the holder determine that the estimated guaranty payment following a deed-in-lieu of foreclosure or compromise would not exceed the estimated payment if the loan proceeded to foreclosure. VA believes there will almost always be cost savings associated with deeds-in-lieu of foreclosure and compromise sales, and therefore will not require the holder to perform an additional calculation as part of the approval process. Cost savings will typically accrue from the reduced cost of a deed versus a foreclosure action, the likelihood that the borrower will be more cooperative in vacating a home after giving a deed instead of being foreclosed upon, and the probability that the home will be in better condition after the borrower gives a deed and arranges an orderly transfer of custody to the holder or VA's agent, rather than the property being abandoned due to foreclosure and subject to possible vandalism. In the case of a compromise claim, VA's requirement that the credit to the indebtedness equals or exceeds the net value of the property will generally ensure cost savings as compared to foreclosure, but even in the rare case when this does not occur, the benefit to the veteran of avoiding foreclosure through a private sale of the home is more than enough to justify acceptance of a compromise offer. The final rule in § 36.4822 incorporates the changes discussed in this section along with those not changed from the proposed rule.

36.4823 Election to Convey Security

Comment: VA should clarify the procedures and implications of debt reductions used to ensure that a property is eligible for conveyance to VA.

VA Response: VA has revised the applicable portions of the new final rule in § 36.4823 to clarify the procedures to be followed to reduce debts in order to gain the right to convey to VA properties acquired at liquidation sales. Under the law (38 U.S.C. 3732(c)), if the calculation by the holder shows that the net value is less than the unguaranteed portion of the loan (i.e., the eligible indebtedness minus VA's maximum claim payable under the guaranty), then the property may not be conveyed to VA. VA has had a longstanding policy, however, of allowing holders to bring such a conveyance into statutory compliance by ''buying down'' the debt to a level where the unguaranteed portion of indebtedness is less than the net value. In these situations, holders must waive any liability a veteran might have otherwise with regard to the amount of indebtedness bought down.

This policy would have continued under the proposal, but it would have been the holder, rather than VA, that was responsible for calculating the buy-down, if any, prior to a liquidation sale. VA received a number of comments expressing concern about the impact that any miscalculation would have on the holder, the servicer, and the veteran, and has therefore revised the final rule in § 36.4823, so that a holder may wait until after the liquidation sale to determine the amount that must be bought down. To make sure the veteran is fully informed, the holder will be required to send the borrower notice no later than 15 calendar days after receipt of VA's guaranty claim payment that the indebtedness in excess of the net value and VA's claim payment has been waived. In addition, VA is revising the final rule in § 36.4838 to designate the conveyance as of an administrative or procedural nature to allow for reasonable accommodations.

Comment: VA should withdraw the proposal to require three year warranties when conveying property to VA, due to the additional burden this would place on servicers and foreclosure attorneys, who would bear the cost of insuring title to the property without receiving adequate compensation.

VA Response: VA concurs. VA's goal in the proposed § 36.4320(c) was to standardize and reduce the documentation required as evidence of acceptable title on properties conveyed to the Secretary. The comments received to the proposed rule provided additional insight on many aspects of the present processes that were not clearly evident to VA previously. For example, in many jurisdictions VA was paying for title insurance policies, but had little occasion to seek indemnity under those policies and believed that purchasing title policies was not cost effective. However, the comments disclosed that many title issues were resolved through the title examination required prior to issuance of the policies. Moreover, many attorneys commented that the compensation received for their participation in the sale of title insurance served to reduce the cost they charged for foreclosure services. It appears that if VA were to eliminate title insurance as an option to establish acceptability of title on properties conveyed to VA, foreclosure attorney fees would increase and many title issues would not be discovered until well after conveyance, which could cause considerable interruption in VA's resale efforts. Accordingly, VA is withdrawing the proposed requirement for a three year warranty, and will instead attempt to standardize document requirements nationwide as much as possible, which in most cases will still include an owner's title insurance policy issued after loan termination in the name of the Secretary along with minimal other documents, such as the state-specific foreclosure document, the original deed of trust or mortgage, special warranty deed from the holder to the Secretary, an original or a copy of mortgagee's title policy, loan assignments, and appointment of substitute trustee. This information is maintained at the RLC level and will continue to be available in the same manner. Accordingly, the proposal to change § 36.4320(c) to require a three year warranty on a conveyance is not included in the new final rule § 36.4823.

Comment: VA should require and pay for a title insurance policy in connection with a deed-in-lieu of foreclosure.

VA Response: VA concurs. VA agrees that requiring a title policy in connection with a deed-in-lieu of foreclosure is necessary and would expedite the process of conveying a property to VA and the subsequent marketing of that property. Therefore, VA is revising the final rule in § 36.4823(c)(4) to provide reimbursement for a title policy when a property is subsequently conveyed to VA by deed-in-lieu of foreclosure.

36.4824 Guaranty Claims; Subsequent Accounting

Comment: VA should incorporate in its rule that any errors found in post claim audits will not be extrapolated over a servicer's prior claim submissions in an effort to recover claim payments that have not been actually identified.

VA Response: VA does not concur, as VA does not believe that such a restrictive rule in § 36.4824 would be in the best interests of the taxpayers supporting the VA home loan program. Extrapolation is basically the practice of reviewing a small sample of cases, determining an error rate, and then applying that error rate across an entire population of claims. While VA does not expect to routinely extrapolate in such a manner, this is a generally accepted tool of auditing that must be preserved.

Before VA would reach the point of exercising this option, it would first follow-up with a holder/servicer to address errors that occurred on a routine basis, and would provide extensive notice of errors discovered that might lead to the extrapolation of errors across all claim submissions. VA does not expect that extrapolation will be applied except in the most egregious cases. Hence, we make no changes based on this comment.

Comment: VA should not impose a one-year deadline for filing claims, or should at least make the penalty more reasonable, because the penalty far outweighs the impact of late filing. In addition, VA should wait until the end of any redemption period before starting the one-year deadline.

VA Response: VA does not concur. The proposed rule § 36.4321(d) required submission of a claim under guaranty no later than one year after the liquidation sale. To ensure accuracy in the Federal budget process, VA needs to know within a reasonable time that specific loans for particular cohort years have been terminated and that costs will be incurred. With the highly automated processes that are being implemented, VA believes that holders should be able to ascertain all necessary information and submit a claim within one year of the completion of the loan termination process, even if a redemption period exists in the particular jurisdiction. However, if there is some valid reason why an individual claim is not timely submitted, we will reserve the right to pay a late claim. Accordingly, VA § 36.4838(a)(3) includes the failure to timely file a claim as a provision of an administrative or procedural nature that may be waived by an official named in § 36.4845. The final rules in § 36.4321(f) and § 36.4824(d) retain the requirement to submit a claim within one year after the liquidation sale. VA § 36.4335 is not modified to include failure to timely file a claim as a provision of an administrative or procedural nature because all servicers will be under the new subpart F requirements in less than one year, so the need to grant relief under subpart B will not be necessary.

36.4828 Partial or Total Loss of Guaranty or Insurance

Comment: The proposed rules did not discuss any plans to implement penalties for late or faulty reporting.

VA Response: The ability to impose penalties already exists. Final rule § 36.4828, based on current § 36.4325, allows VA to adjust claims to the extent that any failure to comply with a regulation increases the ultimate liability of the Secretary. Therefore, no further provision is needed to establish VA's right to impose a penalty when a servicer's failure causes increased liability to VA. The new final rule § 36.4828(b) is slightly different from the existing § 36.4325(b) in order to improve its structure. In addition, while the proposed rule stated that in § 36.4325 two citations (§ 36.4325(b)(5) and (6)) would be deleted and replaced by one new citation for electronic reporting, in the final rule § 36.4828(b), the one citation for electronic reporting (§ 36.4828(b)(4)) actually replaces what are three citations in the existing § 36.4325(b)(4), (5) and (6).

36.4833 Maintenance of Records

Comment: Servicers should not be required to submit audit documentation to VA in a particular imaged format as a condition of doing business with VA.

VA Response: VA concurs. VA did not intend to require a specific imaging format, but inadvertently did so by citing only three specific formats in the proposed rule. This has been changed in the final § 36.4833 to provide that required documents sent to VA electronically be in .jpg, .gif, .pdf, or a similarly widely accepted format.

Comment: Servicers should not be required to provide imaged documents for audits, as this will greatly increase their costs.

VA Response: VA does not concur. Servicers are presently required by VA policy and the authority in § 36.4330 to submit paper documentation with *all claims* under the guaranty. That involves copying *all documents* related to payments received on a loan, disbursements chargeable thereto, and the dates thereof, including copies of bills and receipts for such disbursements, which may require conversion of electronic documents to paper form. VA proposed instead in § 36.4321(d) that servicers submit the *information* in those documents in an electronic format when filing a claim, while retaining the supporting documents in the event of a post-claim audit by VA. Post-claim audits by VA will typically involve only a percentage sampling of submitted claims, so the number of cases for which documentation will eventually be submitted to VA will be greatly reduced. VA does not specify how servicers must retain documents in order to comply with this or any other regulatory and statutory requirements, but will allow a reasonable period of time for access to the documents upon request. The proposed requirement to submit electronically only the documents on cases selected for post-audit should be much less of a burden on servicers, because even if converting a document to electronic format may be more costly than making a paper copy, the overall reduction in the number of documents that must be submitted should result in lower costs. Therefore, VA finds no basis for changing the proposal in the final rule § 36.4833.

Comment: The proposed exception to allow submission of paper documents based on size of servicing portfolio is confusing.

VA Response: VA concurs and has deleted this exception in the final rule § 36.4833. The fast-paced growth in technology has resulted in its wider availability at ever decreasing costs, so the requirement for electronic submission of documents to VA will not create a significant burden for a servicer of any size.

VA has also corrected erroneous dates that appeared in the proposed § 36.4330(c). When the rule was being drafted it was hoped that it could be effective October 1, 2005, and that date was intended to apply to both types of documentation required, even though the second date was shown as October 1, 2004. In the final § 36.4833 both dates are shown as the effective date of the new rule.

36.4836 [Reserved]

The corresponding § 36.4333 titled ''Satisfaction of indebtedness'' will not be included in subpart F. This is because the new final § 36.4817(c)(1) requires electronic reporting of loans paid in full, thereby obviating the need for instructions on paper notification of payment in full. This § 36.4836 will be shown as reserved for future use.

36.4838 Supplementary Administrative Action

In response to several comments about the need for discretion on the exercise of new authorities in the new subpart F, VA is including in the new final § 36.4838 additional items of an administrative or procedural nature, including some which replace existing items in the corresponding section of subpart B.

36.4848 Servicer Appraisal Processing Program

Comment: Servicers expressed concern about accepting the risk that VA might later determine that values rendered by the Servicer Appraisal Processing Program (SAPP) were too high and then adjust claims or even reconvey properties. Servicers also expressed concern that they would be unable to employ sufficient numbers of staff review appraisers, and instead want to rely only on values provided by VA-approved appraisers.

VA Response: VA believes that servicers should not be concerned about these matters. VA presently prescribes uniform qualifications for appraisers in accordance with 38 U.S.C. 3731. However, that same section requires review by VA of appraisal reports prior to determining the reasonable value of a property that is the security for a VA-guaranteed loan. Public Law 100–198, enacted December 21, 1987, authorized the Lender Appraisal Processing Program (LAPP), which enables VA to permit qualified lenders to review loan-origination appraisals, ensure adherence to VA-published minimum property requirements, and set the reasonable value of properties for purposes of determining the maximum loan VA could guarantee.

VA's experience is that delegating appraisal reviews to lenders under the LAPP has worked well and often expedites the loan-origination process. About 95% of all new appraisals are reviewed under LAPP. The number of appraisals required for loan liquidation purposes is significantly lower than the number related to new loan originations, amounting to about 15% of total appraisals reviewed. With lenders employing enough qualified staff appraisal reviewers to handle 95% of new appraisals, there should be no shortage of reviewers available to handle the much lower volume of liquidation appraisals.

Servicers should have no concerns about VA reconveying properties due to value increases made by staff appraisal reviewers, as VA regulations do not provide for such a practice. As contained in the proposed rule, the final rule in §§ 36.4344a(d) and 36.4848(d) does retain the right for VA to be indemnified for additional loss caused by an increase in value made by the servicer that was unwarranted, or arbitrary and capricious. The final rule in §§ 36.4344a(h) and 36.4848(h) also retains provisions to withdraw, for proper cause, authority of servicers to determine reasonable values, such as determination of a pattern of appraisal reviews being conducted in a careless or negligent manner, especially after being called to the servicer's attention. Such withdrawal of authority would simply return servicers to the position of waiting for VA staff appraisers to review liquidation appraisals and establish reasonable values, rather than being able to more quickly establish fair market value and determine the net value of the property for liquidation purposes. Accordingly, we make no changes based on this comment.

36.4850 Servicing Procedures for Holders

Comment: VA should adjust the timeframe for reporting abandoned properties in relation to the date on which inspections will be required. VA should also retain the 15-day reporting schedule rather than the proposed 5-day rule.

VA Response: VA concurs. In the proposed § 36.4346(i) VA intended simply to ensure prompt notice when a holder learns of an abandoned property, which could occur prior to verification through a required property inspection. However, VA agrees that the majority of notices about abandoned property will be the result of property inspections, which will not typically be received until a loan is at least 60 days delinquent, and is therefore changing the final rule accordingly. Reporting of this event will fall under the provisions of the final rule in 38 CFR 36.4817(c)(10), which will require reporting no later than the 7th calendar day of the month following the month the occupancy status change was verified.

Comment: VA should reconsider the requirements related to abandonment and extraordinary waste or hazard.

VA Response: VA concurs. Since the time of the proposed rule change to § 36.4346(i)(2), events such as Hurricane Katrina have demonstrated the difficulty in mandating loan termination due to the appearance of the potential for extraordinary waste. VA has even issued guidance to holders following Katrina to exercise additional caution before deciding that a property in a major disaster area could be subject to additional waste because of an apparent lack of care, since many people were displaced without the resources to quickly return and attempt repairs to their homes. Therefore, VA is deleting that part of the proposed rule that would have added ''extraordinary waste or hazard''.

The first two sentences of the existing rule § 36.4346(i)(2) describe actions to be taken when a holder obtains information that ''indicates'' a property may be abandoned, and the proposed rule change was primarily to conform reporting requirements to the proposed rule § 36.4315a. VA believes that while the term abandoned may be somewhat subjective, there are obvious situations, such as when the borrower mails in the keys and advises the holder that no further payments will be made, in which a holder will have no doubt that the property is abandoned. The existing rule calls for action that should lead to confirmation of whether or not a property is actually abandoned. Thus, the final rule in § 36.4850(i)(2) will retain the mandate to report abandonment in accordance with § 36.4817(c)(10) as a change in occupancy status and initiate termination when abandonment has been confirmed.

Comment: In changing the requirement for provision of an annual statement for income tax purposes, VA should be consistent with Internal Revenue Service (IRS) requirements.

VA Response: VA concurs. It was VA's intent in the proposed revision to § 36.4346(c) to change from 60 days to 30 days to achieve that consistency. However, the comment pointed out that IRS requires annual statements be sent no later than January 31st of each year, so VA's requirement of 30 days would be different. Accordingly, the final rule § 36.4850(c) has been changed to require an annual statement be provided before February 1st of each calendar year.

36.4979 Payment of Insurance

As with § 36.4809, this requires a conforming amendment in the final rule. The existing rule in § 36.4374 refers to a time period specified in § 36.4316, which is three months. Because reporting and processing of defaults are handled differently in the new rules in §§ 36.4800 through 36.4893, inclusive, there is not a similar waiting period specified in § 36.4818. Therefore, the final rule in § 36.4879 will replace the reference to another section with the actual time frame of three months. There is a similar situation with a reference in § 36.4374 to reporting under § 36.4317, and in this case the final rule in § 36.4879 will refer to the applicable reporting required by §§ 36.4817 and 36.4850.

Restructuring of and Authority for Part 36

In order to make it easier to refer to the new §§ 36.4800 through 36.4893, inclusive, VA is designating those sections as subpart F of part 36. VA is grouping other portions of part 36 into appropriate subparts as shown in this notice. Also, to make it easier to identify the appropriate authority for each section of the new subpart F, VA is revising the citation for the authority of part 36 to refer only to the general authorities, and is including the specific appropriate authority for each section in the new subpart F.

Administrative Procedures Act

Pursuant to 5 U.S.C. 553(d)(3), we find that there is good cause to dispense with the 30-day delayed effective date requirement. The public has received extensive knowledge of the changes effected by the new rules through the initial publication of the proposed rules and two supplemental notices of revisions to the initial proposals, and VA has received advice that the public is anxious for the new rules to be effective.

One of the primary changes in the new rules is the implementation of electronic reporting of information on VA-guaranteed home loans. Due to the extensive time required for information technology system changes, industry participants in the VA home loan program initiated development work on the system changes soon after the first supplemental notice provided sufficient details. The first industry segment under the planned phased implementation is prepared to begin operations under the proposed changes immediately upon publication of the new rules, and any delays in implementation would create financial burdens as they continue to operate under the old rules while maintaining additional system capability for operations under the new rules. Moreover, all other industry segments will not be subject to these electronic reporting rules for more than 30 days after these rules become effective, and therefore the 30-day delayed effective date would not affect any segment other than the first. VA is also prepared to accept electronic reporting upon publication of the new rules, and veterans will begin to benefit from the new rules as soon as they are effective. Any delays will be financially costly to the Government, both in terms of additional contracting support required until final implementation, and with respect to the loss of savings expected for the program under the new rules.

The changing economic situation, with increasing numbers of foreclosures nationwide, also contributes to the need for immediate implementation of the new rules for several reasons. The new environment for servicing VA-guaranteed home loans created by these rules will encourage earlier additional loss mitigation efforts by private servicers in place of the present Government outreach at later stages of loan default. These earlier efforts should result in more veterans being able to reinstate delinquent loans and avoiding foreclosure. This will also result in fewer claims paid by VA, while the claims actually paid will be less under the new rules due to the standardized timeframes for completing termination in those cases where it is unavoidable. In addition, the increased legal fees for termination allowed under the new rules will ensure that VA-guaranteed loans receive the same priority as those of other guarantors, insurers and investors in the termination process, thereby avoiding the costs associated with undue delays.

Due to the issues described above, it is imperative that the new rules become effective immediately upon publication. Accordingly, there is good cause under section 553(d)(3) to dispense with the 30-day delayed effective date requirement.

Paperwork Reduction Act of 1995

This final rule contains provisions that constitute collections of information under the Paperwork Reduction Act (44 U.S.C. 3501–3521). In the preamble of the proposed rule, we described the information collections that would need OMB approval and provided a comment period. OMB has approved those proposed collections and has assigned control numbers 2900–0021, 2900–0045, 2900–0112, 2900–0362, and 2900–0381. OMB assigns control numbers to collections of information it approves. VA may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

Unfunded Mandates

The Unfunded Mandates Reform Act of 1995 requires, at 2 U.S.C. 1532, that agencies prepare an assessment of anticipated costs and benefits before issuing any rule that may result in an expenditure by State, local, and tribal governments, in the aggregate, or by the private sector, of $100 million or more (adjusted annually for inflation) in any given year. This final rule will have no such effect on State, local, and tribal governments, or on the private sector.

Executive Order 12866

Executive Order 12866 directs agencies to assess all costs and benefits of available regulatory alternatives and, when regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety, and other advantages; distributive impacts; and equity). The Executive Order classifies a ''significant regulatory action,'' requiring review by the Office of Management and Budget (OMB) unless OMB waives such review, as any regulatory action that is likely to result in a rule that may: (1) Have an annual effect on the economy of $100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities; (2) create a serious inconsistency or otherwise interfere with an action taken or planned by another agency; (3) materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

The economic, interagency, budgetary, legal, and policy implications of this final rule have been examined, and it has been determined to be a significant regulatory action under Executive Order 12866.

Regulatory Flexibility Act

The Secretary hereby certifies that this final rule would not have a significant economic impact on a substantial number of small entities as they are defined in the Regulatory Flexibility Act, 5 U.S.C. 601 et seq. The vast majority of VA loans are serviced by very large financial companies. Only a handful of small entities service VA loans and they service only a very small number of loans. This rule, which only impacts veterans, other individual obligors with guaranteed loans, and companies that service VA loans, will have very minor impact on a very small number of small entities servicing such loans. Therefore, pursuant to 5 U.S.C. 605(b), this rule is exempt from the initial and final regulatory flexibility analysis requirements of sections 603 and 604.

Catalog of Federal Domestic Assistance

The Catalog of Federal Domestic Assistance program number and title for this program is 64.114, Veterans Housing Guaranteed and Insured Loans.

List of Subjects in 38 CFR Part 36

Condominiums, Handicapped, Housing, Indians, Individuals with disabilities, Loan programs—housing and community development, Loan programs—Indians, Loan programs—veterans, Manufactured homes, Mortgage insurance, Reporting and recordkeeping requirements, Veterans.

Approved: October 24, 2007.

Gordon H. Mansfield,

Acting Secretary of Veterans Affairs.

Editorial Note: This document was received at the Office of the Federal Register on January 23, 2008.

■ For the reasons set out in the preamble, 38 CFR part 36 is amended as set forth below.

PART 36—LOAN GUARANTY

■ 1. The authority citation for part 36 is revised to read as follows:

Authority: 38 U.S.C. 501 and as otherwise noted.

■ 2. Remove the undesignated center heading preceding § 36.4201 and the authority citation directly below that center heading.

■ 3. A heading for subpart A is added preceding § 36.4201 to read as follows:

Subpart A—Guaranty of Loans to Veterans to Purchase Manufactured Homes and Lots, Including Site Preparation

* * * * *

■ 4. Remove the undesignated center heading preceding § 36.4300 and the authority citation directly below that center heading.

■ 5. A heading for subpart B is added preceding § 36.4300 to read as follows:

Subpart B—Guaranty or Insurance of Loans to Veterans

* * * * *

■ 6. Revise § 36.4313(b)(5) to read as follows:

§ 36.4313 Advances and other charges.

* * * * *

(b) * * *

(5)(i) Fees for legal services actually performed, not to exceed the reasonable and customary fees for such services in the State where the property is located, as determined by the Secretary.

(ii) In determining what constitutes the reasonable and customary fees for legal services, the Secretary shall review allowances for legal fees in connection with the foreclosure of single-family housing loans, including bankruptcy-related services, issued by HUD, Fannie Mae, and Freddie Mac. The Secretary will review such fees annually and, as the Secretary deems necessary, publish in the **Federal Register** a table setting forth the amounts the Secretary determines to be reasonable and customary. The table will reflect the primary method for foreclosing in each state, either judicial or non-judicial, with the exception of those States where either judicial or non-judicial is acceptable. The use of a method not authorized in the table will require prior approval from VA. This table will be available throughout the year on a VA controlled Web site, such as at *www.homeloans.va.gov*.

(iii) If the foreclosure attorney has the discretion to conduct the sale or to name a substitute trustee to conduct the sale, the combined total paid for legal fees under paragraph (b)(5)(i) of this section and trustee's fees pursuant to paragraph (b)(4) of this section shall not exceed the applicable maximum allowance for legal fees established under paragraph (b)(5)(ii) of this section. If the trustee conducting the sale must be a Government official under local law, or if an individual other than the foreclosing attorney (or any employee of that attorney) is appointed as part of judicial proceedings, and local law also establishes the fees payable for the services of the public or judicially appointed trustee, then those fees will not be subject to the maximum established for legal fees under paragraph (b)(5)(ii) of this section and may be included in the total indebtedness.

* * * * *

■ 7. Amend § 36.4321 by adding paragraph (f) immediately before the authority citation at the end of the section to read as follows:

§ 36.4321 Computation of guaranty claims; subsequent accounting.

* * * * *

(f)(1)(i) Except as provided in paragraph (f)(1)(ii) of this section, a holder shall file a claim for payment under the guaranty no later than 1 year after the completion of the liquidation sale. For purposes of this section, the liquidation sale will be considered completed when:

(A) The last act required under State law is taken to make the liquidation sale final, but excluding any redemption period permitted under State law;

(B) If a holder accepts a voluntary conveyance of the property in lieu of foreclosure, the date of recordation of the deed to the holder or the holder's designee; or

(C) In the case of a sale of the property to a third party for an amount less than is sufficient to repay the unpaid balance on the loan where the holder has agreed in advance to release the lien in exchange for the proceeds of such sale, the date of settlement of such sale.

(ii) With respect to any liquidation sale completed prior to February 1, 2008, all claims must be submitted no later than February 2, 2009.

(2) If additional information becomes known to a holder after the filing of a guaranty claim, the holder may file a supplemental claim provided that such supplemental claim is filed within the time period specified in paragraph (f)(1) of this section.

(3) No claim under a guaranty shall be payable unless it is submitted within the time period specified in paragraph (f)(1) of this section.

(4) In the event that VA does not approve payment of any item submitted under a guaranty claim, VA shall notify the holder what items are being denied and the reasons for such denial. The holder may, within 30 days after the date of such denial notification, submit a request to VA that one or more items that were denied be reconsidered. The holder must present any additional information justifying payment of items denied.

* * * * *

■ 8. Add § 36.4344a to read as follows:

§ 36.4344a Servicer appraisal processing program (SAPP).

(a) Delegation of authority to servicers to review liquidation appraisals and determine reasonable value. Based on the reasonable value, the servicer will be able to determine net value.

(1) To be eligible for delegation of authority to review VA liquidation appraisals and determine the reasonable value for liquidation purposes on properties secured by VA guaranteed or insured 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 (SAR) acceptable to the Secretary.

(2) To qualify as a servicer's staff appraisal reviewer an applicant must be a full-time member of the servicer'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 SAPP staff appraisal reviewer. Three years of appraisal related experience is necessary to qualify as a servicer's staff appraisal reviewer. That experience must demonstrate 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. The individual must demonstrate the ability to review the work of others and to recognize deviations from accepted appraisal principle, practices, and techniques, error in computations, and unjustifiable and unsupportable conclusions.

(3) Servicers that have a staff appraisal reviewer determined acceptable to VA, will be authorized to review liquidation appraisals and make reasonable value determinations for liquidation purposes on properties that are the security for VA guaranteed or insured loans. Additionally, servicers must satisfy initial 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 loan center in whose jurisdiction the servicer's staff appraisal reviewer is located before the SAPP authority may be utilized by that servicer in any other VA office's jurisdiction. To satisfy the initial office case review requirement, the first five cases of each servicer 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 servicer's notice of value. At that point, and prior to loan termination, each of the five cases will be submitted to the VA regional loan center having jurisdiction over the property. After a staff review of each case, VA will issue a notice of value which the servicer may use to compute the net value of the property for liquidation purposes. If these five cases are found to be acceptable by VA, the servicer's staff appraisal reviewer will be allowed to fully process subsequent appraisals for properties regardless of jurisdictional location without prior submission to VA and issuance by VA of a notice of value. Where the servicer's reviewer cannot readily meet the jurisdictional review requirement, the SAR applicant may request that VA expand the geographic area of consideration. VA will accommodate such requests if practicable. The initial office case review requirement may be expanded by VA if acceptable performance has not been demonstrated. After satisfaction of the initial office case review requirement, routine reviews of SAPP cases will be made by VA staff based upon quality control procedures established by the Under Secretary for Benefits. Such review will be made on a random sampling or performance related basis.

(4) Certifications required from the servicer will be specified with particularity in the separate instructions issued by the Secretary, as noted in paragraph (b) of this section.

(b) *Instructions for SAPP Procedures.* The Secretary will publish separate instructions for processing appraisals under the Servicer 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 SAPP cases. Due diligence is considered by VA to represent that care, as is to be properly expected from, and ordinarily exercised by, a reasonable and prudent servicer who would be dependent on the property as security to protect its investment.

(c) *Adjustment of value recommendations.* The amount of authority to upwardly adjust the fee appraiser's estimated market value during the servicer staff appraisal reviewer's initial review of the appraisal report or to subsequently process an appeal of the servicer's established reasonable value will be specified in the separate instructions issued by VA as noted in § 36.4344a(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.

(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 appraiser's estimated market values or servicer's reasonable value determinations above the amount specified in the separate instructions issued by VA must be submitted, along with the servicer's recommendations, if any, to VA for processing and final determination. Unless otherwise authorized in the separate instructions servicers 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 servicer'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 servicer'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.

(d) *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 servicer under paragraph (c) of this section 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.

(e) *Affiliations.* A servicer affiliated with a real estate firm, builder, land developer or escrow agent as a subsidiary division, or in any other entity in which it has a financial interest or which it owns may not use the authority for any cases involving the affiliate unless the servicer demonstrates to the Secretary's satisfaction that the servicer 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).

(f) *Quality control plans.* The servicer must have an effective self-policing or quality control system to ensure the adequacy and quality of their SAPP 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 servicer's independent internal audit division which reports directly to the firm's chief executive officer. The servicer 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 servicer's application of SAPP authority.

(g) *Fees.* The Secretary will require servicers to pay a $100.00 application fee for each SAR the servicer nominates for approval. The application fee will also apply if the SAR begins work for another servicer.

(h) *Withdrawal of servicer authority.* The authority for a servicer to determine reasonable value may be withdrawn by the Loan Guaranty Officer when proper cause exists. A servicer's authority to make reasonable value determinations shall be withdrawn when the servicer no longer meets the basic requirements for delegating the authority, or when it can be shown that the servicer'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 servicer or the servicer'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 SAPP 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 servicer'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 servicer 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 servicer'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 SAPP processing privileges. However, if within 15 days after receiving notice the servicer requests an opportunity to contest the withdrawal, the servicer 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 Loan Center Director who shall make the determination as to whether the action should be sustained, modified or rescinded. The servicer will be informed in writing of the decision.

(2) The servicer has the right to appeal the Regional Loan Center Director's decision to the Undersecretary for Benefits. In the event of such an appeal, the Under Secretary for Benefits will review all relevant material concerning the matter and make a determination that shall constitute final agency action. If the servicer's submission of opposition raises a genuine dispute over facts material to the withdrawal of SAPP authority, the servicer 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 Under Secretary for Benefits will appoint a hearing officer or panel to conduct the hearing. When such additional proceedings are necessary, the Under Secretary for Benefits shall base the determination on the facts as found, together with any information and argument submitted by the servicer.

(3) In actions based upon a conviction or civil judgment, or in which there is no genuine dispute over material facts, the Under Secretary for Benefits shall make a decision on the basis of all the information in the administrative record, including any submission made by the servicer.

(4) Withdrawal of the SAPP authority will require that VA make subsequent determinations of reasonable value for the servicer. Consequently, VA staff will review each appraisal report and issue a Notice of Value which can then be used by the servicer to compute the net value of properties for liquidation purposes.

(5) Withdrawal by VA of the servicer's SAPP authority does not prevent VA from also withdrawing automatic processing authority or taking debarment or suspension action based upon the same conduct of the servicer.

(Authority: 38 U.S.C. 3731)

■ 9. Remove the undesignated center heading preceding § 36.4400 and the authority citation directly below that center heading.

■ 10. A heading for subpart C is added preceding § 36.4400 to read as follows:

Subpart C—Assistance to Certain Disabled Veterans in Acquiring Specially Adapted Housing

* * * * *

■ 11. Remove the undesignated center heading preceding § 36.4500 and the authority citation directly below that center heading.

■ 12. A heading for subpart D is added preceding § 36.4500 to read as follows:

Subpart D—Direct Loans

* * * * *

■ 13. Remove the undesignated center heading preceding § 36.4600 and the authority citation directly below that center hearing.

■ 14. A heading for subpart E is added preceding § 36.4600 to read as follows:

Subpart E—Sale of Loans, Guarantee of Payment, and Flood Insurance

* * * * *

■ 15. Add subpart F to read as follows:

Subpart F—Guaranty or Insurance of Loans to Veterans With Electronic Reporting

Subpart F—Guaranty or Insurance of Loans to Veterans With Electronic Reporting

§ 36.4800 Applicability of this subpart.

(a) This subpart applies to loans serviced by a mortgage servicing industry segment on or after the date that VA issues a **Federal Register** notice making this subpart applicable to that segment. This includes loans entitled to an automatic guaranty, or otherwise guaranteed or insured, on or after the date assigned in the **Federal Register**, and loans that were 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. 3703(c)(1))

§ 36.4801 Definitions.

Whenever used in 38 U.S.C. chapter 37 or subpart F 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))

Compromise sale. A sale to a third party for an amount less than is sufficient to repay the unpaid balance on the loan where the holder has agreed in advance to release the lien in exchange for the proceeds of such sale.

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

Designated appraiser. 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 person 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 §§ 36.4860 through 36.4865 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) and (f))

Economic readjustment. 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 or 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 § 36.4801, 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. Guaranty means 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 obligation or the authorized servicing agent (also referred to as ''the servicer'') of the lender or of the assignee or transferee.

(Authority: 38 U.S.C. 3714)

Home. Home means place of residence.

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

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

Insurance account. 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. 3703(a).

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 of a loan which is guaranteed or insured by VA.

(Authority: 38 U.S.C. 3703(c)(1) and 3704(d))

Lien. 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. This term also includes a compromise sale.

(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 §§ 36.4800 through 36.4893 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). Net loss on insured loans means the indebtedness, plus any other charges authorized under § 36.4814, 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 an amount representing the costs that the Secretary estimates would be incurred by VA in acquiring and disposing of the property. The number to be subtracted from the fair market value will be calculated by multiplying the fair market value by the current cost factor. The cost factor used will be the most recent percentage of the fair market value that VA calculated and published in the Notices section of the **Federal Register** (it is intended that this percentage will be calculated annually). In computing this cost factor, VA will determine the average operating expenses and losses (or gains) on resale incurred for properties acquired under § 36.4823 which were sold during the preceding fiscal year and the average administrative cost to VA associated with the property management activity. The final net value derived from this calculation will be stated as a whole dollar amount (any fractional amount will be rounded up to the next whole dollar). The cost items included in the calculation 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.* (i) An estimate of the total cost for VA of personnel (salary and benefits) and overhead (which may include things such as travel, transportation, communication, utilities, printing, supplies, equipment, insurance claims and other services) associated with the acquisition, management and disposition of property acquired under § 36.4823 of this part. The average administrative costs will be determined by:

(A) Dividing the total cost for VA personnel and overhead salary and benefits costs 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; and

(B) Dividing the figure calculated in paragraph (3)(i)(A) of this definition by the VBA ratio of personal services costs to total obligations.

(ii) The three cost averages will be added to the average loss (or gain) on property sold during the preceding fiscal year (based on the average property purchase price) and the sum will be divided by the average fair market value at the time of acquisition for properties which were sold during the preceding fiscal year to derive the percentage to be used in estimating net value.

(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 §§ 36.4800 through 36.4893 or for the construction of fixtures or appurtenances thereon or for alterations, improvements, or repairs thereon required by §§ 36.4800 through 36.4893 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), loans 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 §§ 36.4860 through 36.4865 shall also be considered real estate loans.

Reasonable value. 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.

Repayment plan. A repayment plan is a written executed agreement by and between the borrower and the holder to reinstate a loan that is 61 or more calendar days delinquent, by requiring the borrower to pay each month over a fixed period (minimum of three months duration) the normal monthly payments plus an agreed upon portion of the delinquency each month.

Repossession. Repossession 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 §§ 36.4860 through 36.4865;

(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;

(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 this subpart, 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. 3703(c)(1) and 3710(a))

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

Servicer. The authorized servicer is either:

(1) The servicing agent of a holder; or

(2) The holder itself, if the holder is performing all servicing functions on a loan. The servicer is typically the entity reporting all loan activity to VA and filing claims under the guaranty on behalf of the holder. VA will generally issue guaranty claims and other payments to the servicer, who will be responsible for forwarding funds to the

holder in accordance with its servicing agreement. Incentives under § 36.4819 will generally be paid directly to the servicer based on its performance under that section and in accordance with its tier ranking under § 36.4818.

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)

Special forbearance. This is a written agreement executed by and between the holder and the borrower where the holder agrees to suspend all payments or accept reduced payments for one or more months, on a loan 61 or more calendar days delinquent, and the borrower agrees to pay the total delinquency at the end of the specified period or enter into a repayment plan.

Total indebtedness: For purposes of 38 U.S.C. 3732(c), the veteran's ''total indebtedness'' shall be the sum of: the unpaid principal on the loan as of the date of the liquidation sale, accrued unpaid interest permitted by § 36.4824(a) of this part, and allowable advances/other charges permitted to be included in the guaranty claim by § 36.4814 of this part.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4802 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 paragraph (a)(4) of this section, 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 $60,000 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.

(b) With respect to an interest rate reduction refinancing loan guaranteed under 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), or (a)(11), the dollar amount of guaranty may not exceed the greater of the original guaranty amount of the loan being refinanced, or 25 percent of the refinancing loan amount.

(Authority: 38 U.S.C. 3703, 3710)

(c) With respect to a loan for an energy efficient mortgage guaranteed under 38 U.S.C. 3710(d), the amount of the guaranty shall be in the same proportion as would have been provided if the energy efficient improvements were not added to the loan amount, and there shall be no additional charge to the veteran's entitlement as a result of the increased guaranty amount.

(Authority: 38 U.S.C. 3703, 3710)

(d) 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.

(e) Subject to the provisions of § 36.4803(g), 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 $24,000 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 $24,000 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 and the sum remaining may be increased by up to $24,000 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)

(f) For the purpose of computing the remaining guaranty or insurance benefit to which a veteran is entitled, loans guaranteed prior to February 1, 2008 shall be taken into consideration as if made subsequent thereto.

(g) 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 § 36.4803, such loan will not be eligible for insurance.

(h) 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, except where the guaranty has been increased under § 36.4815, or the percentage of the total 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))

(i) 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.

(j) Notwithstanding the provisions of paragraph (i) of this section, in computing the aggregate amount of guaranty or insurance housing loan entitlement available to a veteran under this chapter, the Secretary may exclude the amount of guaranty or insurance housing loan entitlement used for any guaranteed, insured, or direct loan under any one of the following circumstances:

(1)(i) The property which secured the loan has been disposed of by the veteran or has been destroyed by fire or other natural hazard; and

(ii) 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 such loan, the loss has been paid in full.

(2) A veteran-transferee has agreed to assume the outstanding balance on the loan and consented to the use of the veteran-transferee's entitlement, to the extent that the entitlement of the veteran-transferor had been used originally, in place of the veteran-transferor's for the guaranteed, insured, or direct loan, and the veteran-transferee otherwise meets the requirements of this chapter.

(3)(i) The loan has been repaid in full; and

(ii) The loan for which the veteran seeks to use entitlement under this chapter is secured by the same property which secured the loan referred to in the preceding paragraph (j)(3)(i) of this paragraph.

(4) In a case not covered by (j)(1) or (j)(2) of this section, the Secretary may, one time per veteran, exclude entitlement used if:

(i) The loan has been repaid in full and, if the Secretary has suffered a loss on the loan, the loss has been paid in full; or

(ii) The Secretary has been released from liability as to the loan and, if the Secretary has suffered a loss on the loan, the loss has been paid in full.

(k) The Secretary may, in any case involving circumstances that the Secretary deems appropriate, waive one or more of the requirements set forth in paragraph (j)(1) of this section.

(Authority: 38 U.S.C. 3702(b), 3710)

(l)(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), 3703(c)(1))

§ 36.4803 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 not later than 60 days following full disbursement and upon the certification of the lender that:

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

(2) Except for acquisition and improvement loans as defined in § 36.4801, 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 § 36.4804 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. 3703(a), 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), 3703(a)(2))

(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 § 36.4801(c), 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 § 36.4804, 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) For loans not reported within 60 days, evidence of guaranty will be issued only if the loan report is accompanied by a statement signed by a corporate officer of the lending institution which explains why the loan was reported late. The statement must identify the case or cases in issue and must set forth the specific reason or reasons why the loan was not submitted on time. Upon receipt of such a statement evidence of guaranty will be issued. A pattern of late reporting and the reasons therefore will be considered by VA in taking action under § 36.4853.

(g) 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 servicemember, 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 that will prevent the veteran or the spouse of the active duty veteran from occupying the property while the work is being completed. In such a case the veteran or spouse of the active duty veteran must certify that he or she intends to occupy or 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 certification only at the time the loan is closed.

(Authority: 38 U.S.C. 3704(c))

(h) 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 VA. 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 that 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 ''payout'' of the entire loan proceeds.

(Authority: 38 U.S.C. 3702(a), 3710(c))

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

(j) 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.

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

(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 that reads 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 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, 3703(c)(1))

(l) 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 VA-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 VA regulations.

(A) If the assumption is approved and the transfer of the security is completed, then the notice required by this paragraph (l) shall consist of the credit package (unless previously provided in accordance with paragraph (l)(1)(i)(B) of this section) and a copy of the executed deed and/or assumption agreement as required by VA office of jurisdiction. The notice shall be submitted to the Department with the VA receipt for the funding fee provided for in § 36.4813(e)(2).

(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 VA office of jurisdiction within 30 days. The holder shall make available to that VA office all items used by the holder in making the holder's decision in case the decision is appealed to VA. If the application remains disapproved after 60 days (to allow time for appeal to and review by VA), then the holder must refund $50 of any fee previously collected under the provisions of § 36.4813(d)(8). 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 (l)(1)(i)(A) of this section.

(C) In performing the requirements of paragraphs (l)(1)(i)(A) or (l)(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 that are documented as beyond the control of the holder, such as employers or depositories not responding to requests for verifications, which were timely forwarded, or follow-ups on those requests.

(ii) If neither the holder nor its authorized servicing agent is an automatic lender, the notice to VA 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 VA 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 (l)(l)(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 § 36.4813(d)(8) 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 § 36.4813(d)(8) must be refunded following the expiration of the 30-day appeal period set out in paragraph (l)(l)(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 (l)(l)(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 (l).

(Authority: 38 U.S.C. 3714)

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0516.)

§ 36.4804 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4805 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.

(Authority: 38 U.S.C. 3703(c)(1) and (d))

§ 36.4806 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 § 36.4802(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))

(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 § 36.4813(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 § 36.4813(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 § 36.4813; and

(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 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 § 36.4802(a).

(Authority: 38 U.S.C. 3703(a), 3710)

§ 36.4807 Interest rate reduction refinancing loan.

(a) Pursuant to 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), and (a)(11), a veteran may refinance an existing VA guaranteed, insured, or direct loan to reduce the interest rate payable on the existing loan provided that all of the following requirements are met:

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

(2) The veteran owns the dwelling or farm residence securing the loan and

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

(ii) Previously occupied the dwelling or residence as his or her home and certifies, in such form as the Secretary shall require, that he or she has previously occupied the dwelling or residence as a home; or

(iii) In a case in which the veteran is or was unable to occupy the residence or dwelling as a home because the veteran was on active duty status as a member of the Armed Forces, the spouse of the veteran occupies, or previously occupied, the dwelling or residence as the spouse's home and certifies to that occupancy in such form as the Secretary shall require.

(Authority: 38 U.S.C. 3710(e)(1))

(3) The monthly principal and interest payment on the new loan is lower than the principal and interest payment on the loan being refinanced; or the term of the new loan is shorter than the term of the loan being refinanced; or the new loan is a fixed-rate loan that refinances a VA-guaranteed adjustable rate mortgage; or the increase in the monthly payments on the loan results from the inclusion of energy efficient improvements, as provided by § 36.4839(a)(4); or the Secretary approves the loan in advance after determining that the new loan is necessary to prevent imminent foreclosure and the veteran qualifies for the new loan under the credit standards contained in § 36.4840.

(4) The amount of the refinancing loan does not exceed:

(i) An amount equal to the balance of the loan being refinanced, which is not delinquent, except as provided in paragraph (a)(5) of this section, plus closing costs authorized by § 36.4813(d) and a discount not to exceed 2 percent of the loan amount; or

(ii) In the case of a loan to refinance an existing VA-guaranteed or direct loan and to improve the dwelling securing such loan through energy efficient improvements, the amount referred to with respect to the loan under paragraph (a)(4)(i) of this section, plus the amount authorized by § 36.4839(a)(4).

(Authority: 38 U.S.C. 3703, 3710)

(5) If the loan being refinanced is delinquent (delinquent means that a scheduled monthly payment of principal and interest is more than 30 days past due), the new loan will be guaranteed only if the Secretary approves it in advance after determining that the borrower, through the lender, has provided reasons for the loan deficiency, has provided information to establish that the cause of the delinquency has been corrected, and qualifies for the loan under the credit standards contained in § 36.4840. In such cases, the term ''balance of the loan being refinanced'' shall include any past due installments, plus allowable late charges.

(6) The dollar amount of guaranty on the 38 U.S.C. 3710(a)(8) or (a)(9)(B)(i) loan does not exceed the greater of the original guaranty amount of the loan being refinanced or 25 percent of the new loan.

(7) The term of the refinancing loan (38 U.S.C. 3710(a)(8)) may not exceed the original term of the loan being refinanced 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. 3703(c)(1), 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 § 36.4802(a). The veteran's loan guaranty entitlement originally used for a purpose as enumerated in 38 U.S.C. 3710(a)(1) through (7) and (a)(9)(A)(i) and (ii) and subsequently transferred to an interest rate reduction refinancing loan (38 U.S.C. 3710(a)(8) or (a)(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 § 36.4802(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 § 36.4854.

(Authority: 38 U.S.C. 3710(a)(8), (a)(9)(B)(i) and (e))

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0601.)

§ 36.4808 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.

(Authority: 38 U.S.C. 3703)

§ 36.4809 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 § 36.4826; 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) With respect to each such loan at least one of the instruments used in the transaction shall contain the following statement: ''This loan is not assumable without the approval of the Department of Veterans Affairs or its authorized agent.'' This statement must be:

(i) Printed in a font size which is the larger of:

(A) Two times the largest font size contained in the body of the instrument; or

(B) 18 points; and

(ii) Contained in at least one of the following:

(A) The note;

(B) The mortgage or deed of trust; or

(C) A rider to either the note, the mortgage, or the deed of trust.

(Authority: (38 U.S.C. 3714(d))

(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 (a)(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 amount 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 § 36.4850(i)(2), or if there exist conditions justifying the appointment of a receiver for the property (without reference to any contractual provisions for such appointment), 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 of such obligation at any time after the continuance of any default for the period of three months.

(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 the prior approval of the Secretary is obtained to do otherwise, or unless 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))

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0516.)

§ 36.4810 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 percent 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 § 36.4815.

(b) Any plan of repayment on loans required to be amortized which does not provide for 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* § 36.4837.

(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))

§ 36.4811 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.

(Authority: 38 U.S.C. 3703(d))

§ 36.4812 Interest rates.

(a) In guaranteeing or insuring loans under 38 U.S.C. chapter 37, the Secretary may elect to require that such loans either bear interest at a rate that is agreed upon by the veteran and the lender, or bear interest at a rate not in excess of a rate established by the Secretary. The Secretary may, from time to time, change that election by publishing a notice in the **Federal Register**. However, the interest rate of a loan for the purpose of an interest rate reduction under 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), or (a)(11) must be less than the interest rate of the VA loan being refinanced. This paragraph does not apply in the case of an adjustable rate mortgage being refinanced under 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), or (a)(11) with a fixed rate loan.

(Authority: 38 U.S.C. 3703, 3710)

(b) For loans bearing an interest rate agreed upon by the veteran and the lender, the veteran may pay reasonable discount points in connection with the loan. The discount points may not be included in the loan amount, except for interest rate reduction refinancing loans under 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), and (a)(11). For loans bearing an interest rate agreed upon by the veteran and the lender, the provisions of § 36.4813(d)(6) and (d)(7) do not apply.

(Authority: 38 U.S.C. 3703, 3710)

(c) Except as provided in § 36.4815, 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.

(Authority: 38 U.S.C. 3710)

(d) Effective October 1, 2003, adjustable rate mortgage loans which comply with the requirements of this paragraph (d) are eligible for guaranty.

(1) *Interest rate index.* Changes in the interest rate charged on an adjustable rate mortgage must correspond to changes in the weekly average yield on one year (52 weeks) Treasury bills adjusted to a constant maturity. Yields on one year Treasury bills at ''constant maturity'' are interpolated by the United States Treasury from the daily yield curve. This curve, which relates the yield on the security to its time to maturity, is based on the closing market bid yields on actively traded one year Treasury bills in the over-the-counter market. The weekly average one year constant maturity Treasury bill yields are published by the Federal Reserve Board of the Federal Reserve System. The Federal Reserve Statistical Release Report H. 15 (519) is released each Monday. These one year constant maturity Treasury bill yields are also published monthly in the Federal Reserve Bulletin, published by the Federal Reserve Board of the Federal Reserve System, as well as quarterly in the Treasury Bulletin, published by the Department of the Treasury.

(2) *Frequency of interest rate changes.* Interest rate adjustments must occur on an annual basis, except that the first adjustment may occur no sooner than 36 months from the date of the borrower's first mortgage payment. The adjusted rate will become effective the first day of the month following the adjustment date; the first monthly payment at the new rate will be due on the first day of the following month. To set the new interest rate, the lender will determine the change between the initial (i.e., base) index figure and the current index figure. The initial index figure shall be the most recent figure available before the date of mortgage loan origination. The current index figure shall be the most recent index figure available 30 days before the date of each interest rate adjustment.

(3) *Method of rate changes.* Interest rate changes may only be implemented through adjustments to the borrower's monthly payments.

(4) *Initial rate and magnitude of changes.* The initial contract interest rate of an adjustable rate mortgage shall be agreed upon by the lender and the veteran. Annual adjustments in the interest rate shall correspond to annual changes in the interest rate index, subject to the following conditions and limitations:

(i) No single adjustment to the interest rate may result in a change in either direction of more than one percentage point from the interest rate in effect for the period immediately preceding that adjustment. Index changes in excess of one percentage point may not be carried over for inclusion in an adjustment in a subsequent year. Adjustments in the effective rate of interest over the entire term of the mortgage may not result in a change in either direction of more than five percentage points from the initial contract interest rate.

(ii) At each adjustment date, changes in the index interest rate, whether increases or decreases, must be translated into the adjusted mortgage interest rate, rounded to the nearest one-eighth of one percent, up or down. For example, if the margin is 2 percent and the new index figure is 6.06 percent, the adjusted mortgage interest rate will be 8 percent. If the margin is 2 percent and the new index figure is 6.07 percent, the adjusted mortgage interest rate will be 8 1/8 percent.

(5) *Pre-loan disclosure.* The lender shall explain fully and in writing to the

borrower, at the time of loan application, the nature of the obligation taken. The borrower shall certify in writing that he or she fully understands the obligation and a copy of the signed certification shall be placed in the loan folder and furnished to VA upon request.

(i) The fact that the mortgage interest rate may change, and an explanation of how changes correspond to changes in the interest rate index;

(ii) Identification of the interest rate index, its source of publication and availability;

(iii) The frequency (i.e., annually) with which interest rate levels and monthly payments will be adjusted, and the length of the interval that will precede the initial adjustment; and

(iv) A hypothetical monthly payment schedule that displays the maximum potential increases in monthly payments to the borrower over the first five years of the mortgage, subject to the provisions of the mortgage instrument.

(6) *Annual disclosure*. At least 25 days before any adjustment to a borrower's monthly payment may occur, the lender must provide a notice to the borrower which sets forth the date of the notice, the effective date of the change, the old interest rate, the new interest rate, the new monthly payment amount, the current index and the date it was published, and a description of how the payment adjustment was calculated. A copy of the annual disclosure shall be made a part of the lender's permanent record on the loan.

(Authority: 38 U.S.C. 3707A)

§ 36.4813 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 this subpart, 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 Department of Veterans Affairs 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 § 36.4829.

(vi) Survey, if required by lender or veteran; except that any charge for a survey in connection with a loan under §§ 36.4860 through 36.4865 (Condominium Loans) must have the prior approval of the Secretary.

(vii) Title examination and title insurance, if any.

(viii) The actual amount charged for flood zone determinations, including a charge for a life-of-the-loan flood zone determination service purchased at the time of loan origination, if made by a third party who guarantees the accuracy of the determination. A fee may not be charged for a flood zone determination made by a Department of Veterans Affairs appraiser or for the lender's own determination.

(ix) Such other items as may be authorized in advance by the Under Secretary for Benefits as appropriate for inclusion under this paragraph (d) 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 consideration, alteration, improvement or repair loans, including supplemental loans made pursuant to § 36.4859, 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) 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), (a)(8), (a)(9)(B)(i) or (a)(9)(B)(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) Discounts shall be computed as follows:

(i) Unless otherwise approved by the Secretary, the discount, if any, to be paid by the borrower on a loan secured by a first lien 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 ½ 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) The borrower, subject to the limitations set forth in paragraphs (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; and

(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 § 36.4801) 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.

Note to paragraph (d)(7)(iii): Acquisition and improvement loans may be closed either on the automatic or prior approval basis.

(iv) Unless the Under Secretary for Benefits otherwise directs, all powers of the Secretary under paragraphs (d)(6) and (7) of this section are hereby delegated to the officials designated by § 36.4845(b).

(Authority: 38 U.S.C. 3703, 3710; 42 U.S.C. 4001 note, 4012a)

(8) On any loan to which 38 U.S.C. 3714 applies, the holder may charge a reasonable fee, not to exceed the lesser of $300 and the actual cost of any credit report required, or any maximum prescribed by applicable State law, for processing an application for assumption and changing its records.

(Authority: 38 U.S.C. 3714)

(e) Subject to the limitations set out in paragraph (e)(4) of this section, a fee must be paid to the Secretary.

(1) The fee on loans to veterans shall be as follows:

(i) On all interest rate reduction refinancing loans guaranteed under 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), and (a)(11), the fee shall be 0.50 percent of the total loan amount.

(ii) On all refinancing loans other than those described in paragraph (e)(1)(i) of this section, the funding fee shall be 2.75 percent of the loan amount for loans to veterans whose entitlement is based on service in the Selected Reserve under the provisions of 38 U.S.C. 3701(b)(5), and 2 percent of the loan amount for loans to all other veterans; provided, however, that if the veteran is using entitlement for a second or subsequent time, the fee shall be 3 percent of the loan amount.

(iii) Except for loans to veterans whose entitlement is based on service in the Selected Reserve under the provisions of 38 U.S.C. 3701(b)(5), the funding fee shall be 2 percent of the total loan amount for all loans for the purchase or construction of a home on which the veteran does not make a down payment, unless the veteran is using entitlement for a second or subsequent time, in which case the fee shall be 3 percent. On purchase or construction loans on which the veteran makes a down payment of 5 percent or more, but less than 10 percent, the amount of the funding fee shall be 1.50 percent of the total loan amount. On purchase or construction loans on which the veteran makes a down payment of 10 percent or more, the amount of the funding fee shall be 1.25 percent of the total loan amount.

(iv) On loans to veterans whose entitlement is based on service in the Selected Reserve under the provisions of 38 U.S.C. 3701(b)(5), the funding fee shall be 2.75 percent of the total loan amount on loans for the purchase or construction of a home on which the veteran does not make a down payment, unless the veteran is using entitlement for a second or subsequent time, in which case the fee shall be 3 percent. On purchase or construction loans on which veterans whose entitlement is based on service in the Selected Reserve make a down payment of 5 percent or more, but less than 10 percent, the amount of the funding fee shall be 2.25 percent of the total loan amount. On purchase or construction loans on which such veterans make a down payment of 10 percent or more, the amount of the funding fee shall be 2 percent of the total loan amount.

(v) All or part of the 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)

(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 38 U.S.C. 3714 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)

(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 paragraph (e)(4) 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 lender is required to pay to the Secretary electronically through the Automated Clearing House (ACH) system the fees described in paragraphs (e)(1) and (e)(2) of this section and any late fees and interest due on them. This shall be paid to a collection agent by operator-assisted telephone, terminal entry, or CPU-to-CPU transmission. The collection agent will be identified by the Secretary. The lender shall provide the collection agent with the following: authorization for payment of the funding fee (including late fees and interest) along with the following information: VA lender ID number; four-digit personal identification number; dollar amount of debit; VA loan number; OJ (office of jurisdiction) code; closing date; loan amount; information about whether the payment includes a shortage, late charge, or interest; veteran name; loan type; sale amount; down payment; whether the veteran is a reservist; and whether this is a subsequent use of entitlement. For all transactions received prior to 8:15 p.m. on a workday, VA will be credited with the amount paid to the collection agent at the opening of business the next banking day.

(Authority: 38 U.S.C. 3729(a))

(5) The fees 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)

(The Office of Management and Budget has approved the information collection requirements in this section under control numbers 2900–0474 and 2900–0516.)

§ 36.4814 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. 3703, 3714, 3732)

(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; may charge against gross amounts collected; may include in any accounting to the Secretary after payment of a claim under the guaranty; may include in the computation of a claim under the guaranty, if lawfully authorized by the loan agreement and subject to § 36.4824(a); or, may include 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 proper 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)(i) Fees for legal services actually performed, not to exceed the reasonable and customary fees for such services in the State where the property is located, as determined by the Secretary.

(ii) In determining what constitutes the reasonable and customary fees for legal services, the Secretary shall review allowances for legal fees in connection with the foreclosure of single-family housing loans, including bankruptcy-related services, issued by HUD, Fannie Mae, and Freddie Mac. The Secretary will review such fees annually and, as the Secretary deems necessary, publish in the **Federal Register** a table setting forth the amounts the Secretary determines to be reasonable and customary. The table will reflect the primary method for foreclosing in each state, either judicial or non-judicial, with the exception of those States where either judicial or non-judicial is acceptable. The use of a method not authorized in the table will require prior approval from VA. This table will be available throughout the year on a VA controlled Web site, such as at *http://www.homeloans.va.gov*.

(iii) If the foreclosure attorney has the discretion to conduct the sale or to name a substitute trustee to conduct the sale, the combined total paid for legal fees under paragraph (b)(5)(i) of this section and trustee's fees pursuant to paragraph (b)(4) of this section shall not exceed the applicable maximum allowance for legal fees established under paragraph (b)(5)(ii) of this section. If the trustee conducting the sale must be a Government official under local law, or if an individual other than the foreclosing attorney (or any employee of that attorney) is appointed as part of judicial proceedings, and local law also establishes the fees payable for the services of the public or judicially appointed trustee, then those fees will not be subject to the maximum established for legal fees under paragraph (b)(5)(ii) of this section and may be included in the total indebtedness.

(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), 3732)

(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 by VA to be necessary and proper in order to preserve or protect the security may be authorized by employees designated in § 36.4845(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) or (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.

(f)(1) Fees and charges otherwise allowable by this section that accrue after the date specified in paragraph (f)(2) of this section may not be included in a claim under the guaranty.

(2) The date referenced in paragraph (f)(1) of this section will be computed by adding 210 calendar days to the due date of the last paid installment, plus the reasonable period that the Secretary has determined, pursuant to § 36.4822(a), it should have taken to complete the foreclosure. There will also be added to the time period specified in the previous sentence such additional time as the Secretary determines was reasonably necessary to complete the foreclosure if the Secretary determines the holder was unable to complete the foreclosure within the time specified in that section due to Bankruptcy proceedings, appeal of the foreclosure by the debtor, the holder granting forbearance in excess of 30 days at the request of the Secretary, or other factors beyond the control of the holder.

(Authority: 38 U.S.C. 3703(c), 3720, 3732)

§ 36.4815 Loan modifications.

(a) Subject to the provisions of this section, the terms of any guaranteed loan may be modified by written agreement between the holder and the borrower, without prior approval of the Secretary, if all of the following conditions are met:

(1) The loan is in default;

(2) The event or circumstances that caused the default has been or will be resolved and it is not expected to re-occur;

(3) The obligor is considered to be a reasonable credit risk, based on a review by the holder of the obligor's creditworthiness under the criteria specified in § 36.4840, including a current credit report. The fact of the recent default will not preclude the holder from determining the obligor is now a satisfactory credit risk provided the holder determines that the obligor is able to resume regular mortgage installments when the modification becomes effective based upon a review of the obligor's current and anticipated income, expenses, and other obligations as provided in § 36.4840;

(4) At least 12 monthly payments have been paid since the closing date of the loan;

(5) The current owner(s) is obligated to repay the loan, and is party to the loan modification agreement; and

(6) The loan will be reinstated to performing status by virtue of the loan modification.

(b) Without the prior approval of the Secretary, a loan can be modified no more than once in a 3-year period and no more than three times during the life of the loan.

(c) All modified loans must bear a fixed-rate of interest, which may not exceed the Government National Mortgage Association (GNMA) current month coupon rate that is closest to par (100) plus 50 basis points. The rate shall be determined as of the close of business the last business day of the month preceding the date the holder approved the loan modification.

(d) The unpaid balance of the modified loan may be re-amortized over the remaining life of the loan. The loan term may extend the maturity date to the shorter of:

(1) 360 months from the due date of the first installment required under the modification, or

(2) 120 months after the original maturity date of the loan.

(e) Only unpaid principal; accrued interest; deficits in the taxes and insurance impound accounts; and advances required to preserve the lien position, such as homeowner association fees, special assessments, water and sewer liens, etc., may be included in the modified indebtedness. Late fees and other charges may not be capitalized.

(f) Holders shall not charge a processing fee under any circumstances to complete a loan modification. However, late fees and any other actual costs incurred and legally chargeable, including but not limited to the cost of a title insurance policy for the modified loan, but which cannot be capitalized in the modified indebtedness, may be collected directly from the borrower as part of the modification process.

(g) Holders will ensure the first lien status of the modified loan.

(h) The dollar amount of the guaranty may not exceed the greater of:

(1) The original guaranty amount of the loan being modified (but if the modified loan amount is less than the original loan amount, then the amount of guaranty will be equal to the original guaranty percentage applied to the modified loan), or

(2) 25 percent of the loan being modified subject to the statutory maximum specified at 38 U.S.C. 3703(a)(1)(B).

(i) The obligor may not receive any cash back from the modification.

(j) This section does not create a right of a borrower to have a loan modified, but simply authorizes the loan holder to modify a loan in certain situations without the prior approval of the Secretary.

(Authority: 38 U.S.C. 3703(c)(1), 3720)

§ 36.4816 Acceptability of partial payments.

A partial payment is a remittance by or on behalf of the borrower on a loan in default (as defined in § 36.4801) 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.

(a) Except as provided in paragraph (b) 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.

(b) 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:

(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 escrows and late charge, if applicable, unless the lesser payment amount has been agreed to under a documented repayment plan;

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

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

(5) 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;

(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 by the taking of the first action required for foreclosure under local law; or

(8) The holder's lien position would be jeopardized by acceptance of the partial payment.

(c) 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 § 36.4828(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))

§ 36.4817 Servicer reporting requirements.

(a) Servicers of loans guaranteed by the Secretary shall report the information required by this section to the Secretary electronically. The Secretary shall accept electronic submission from each entity servicing loans guaranteed under 38 U.S.C. chapter 37 not later than the effective date of this rule.

(b) Not later than the seventh calendar day of each month each servicer shall report to the Secretary basic information (loan identification information, payment due date, and unpaid principal balance) for every loan guaranteed by the Secretary currently being serviced by that entity, unless previously reported under paragraph (c)(7) of this section and has not reinstated, terminated, or paid in full.

(c) Servicers shall report to the Secretary the following specific loan events in accordance with the timeframes described for each event. Unless otherwise specified herein, the servicer shall report these events on a monthly basis (i.e., no later than the 7th calendar day of the month following the month in which the event occurred) only for delinquent loans in its portfolio.

(1) Loan paid in full—when the loan obligation has been fully satisfied by receipt of funds and not a servicing transfer. The servicer shall report this event regardless of delinquency status.

(2) Authorized transfer of ownership—when the servicer learns that an authorized transfer of ownership has been completed. The servicer shall report this event regardless of delinquency status.

(3) Release of liability—when an obligor has been released from liability. The servicer shall report this event regardless of delinquency status.

(4) Partial release of security—when the holder has released the lien on a part of the security for the loan pursuant to § 36.4827. The servicer shall report this event regardless of delinquency status.

(5) Servicing transfer (transferring servicer)—when a holder transfers the loan to another servicer.

(6) Servicing transfer (receiving servicer)—when a servicer boards the loan.

(7) Electronic Default Notification (EDN)—when the loan becomes at least 61 days delinquent. The servicer shall report this event no later than the 7th calendar day from when the event occurred. The servicer shall report this event only once per default for delinquent loans in its portfolio.

(8) Delinquency status—when the servicer notifies VA of any updates to the delinquency information on loans for which an EDN has been submitted. The servicer shall report this event monthly (i.e., no later than the 7th calendar day of the month following the month for which the reported information applies) until the default cures or the loan terminates.

(9) Contact information change—when there is a change to the contact information for current owners or a property or mailing address change.

(10) Occupancy status change—when there is a change in property occupancy status.

(11) Bankruptcy filed—when any owner files a petition under the Bankruptcy Code. The servicer shall report this event no later than the 7th calendar day from when the event occurred. The servicer shall report this event only on delinquent loans in its portfolio, if appropriate, or with the EDN when it is reported.

(12) Bankruptcy update—when a significant event related to the bankruptcy has occurred. The servicer shall report this event no later than the 7th calendar day from when the event occurred. The servicer shall report this event only on delinquent loans in its portfolio, if appropriate, or with the EDN when it is reported.

(13) Loss mitigation letter sent—when the servicer sends the loss mitigation letter to the borrower as required by § 36.4850(g)(1)(iv).

(14) Partial payment returned—when the servicer returns a partial payment to the borrower.

(15) Default cured/loan reinstated—when a previously reported default (i.e. an EDN was filed) has cured/loan reinstated.

(16) Default reported to credit bureau—when the servicer notifies the credit bureaus of a defaulted loan or loan termination. The servicer shall report this event only on delinquent loans in its portfolio, and shall report the first occurrence only.

(17) Repayment plan approved—when the servicer approves a repayment plan.

(18) Special forbearance approved—when the servicer approves a special forbearance agreement.

(19) Loan modification approved—when the servicer approves a loan modification.

(20) Loan modification complete—when both the servicer (and/or the holder, where necessary) and the owner(s) have executed the modification agreement.

(21) Compromise sale complete—when a compromise sale closes.

(22) Deed-in-lieu of foreclosure complete—when the servicer records the deed-in-lieu of foreclosure. The servicer shall report this no later than the 7th calendar day from when the event occurred.

(23) Foreclosure referral—when the loan is referred to legal counsel for foreclosure. The servicer shall report this no later than the 7th calendar day from when the event occurred.

(24) Foreclosure sale scheduled—when the foreclosure sale is scheduled. The servicer shall report this no later than the 7th calendar day from when the event occurred.

(25) Results of sale—when the foreclosure sale is complete, the servicer reports the results of the foreclosure sale. The servicer shall report this no later than the 7th calendar day from when the event occurred.

(26) Transfer of custody—when the servicer notifies VA of the holder's intent to convey the property. The servicer shall report this no later than the 15th calendar day from the date of liquidation sale (such as the date of foreclosure sale, date of recordation of a deed-in-lieu of foreclosure, or confirmation/ratification of sale date when required under local practice).

(27) Improper transfer of custody—when the servicer discovers that the conveyance of the property to VA was improper. The servicer shall report this no later than the 7th calendar day from when the error is discovered.

(28) Invalid sale results—when the foreclosure sale is invalid. The servicer shall report this no later than the 7th

calendar day from discovery of the event that invalidated the sale.

(29) Confirmed sale date with no transfer of custody—when the loan is terminated, the property is not conveyed, and the property is located in a confirmation/ratification of sale state.

(30) Basic claim information—when the servicer files a claim under guaranty. The servicer shall report this event within 365 calendar days of loan termination for non-refund claims, and within 60 calendar days of the refund approval date for refund claims.

(31) Refunding Settlement—when VA refunds a loan and the servicer reports the tax and insurance information. The servicer shall report this event within 60 calendar days of the refund approval date.

(Authority: 38 U.S.C. 3703(c), 3732)

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0021.)

§ 36.4818 Servicer tier ranking—temporary procedures.

(a) The Secretary shall assign to each servicer a ''Tier Ranking'' based upon the servicer's performance in servicing guaranteed loans. There shall be four tiers, known as tier one, tier two, tier three, and tier four, with tier one being the highest rated and tier four the lowest. Upon the effective date of this regulation, every servicer of loans guaranteed by the Secretary shall be presumed to be in servicer tier two, and shall remain in tier two until the date specified in paragraph (c)(2) of this section.

(b) For purposes of this section, the term ''calendar quarter'' shall mean the 3-month periods ending on March 31, June 30, September 30, and December 31.

(c)(1) No later than 30 calendar days after the last business day of the first calendar quarter occurring after the rules for determining tier rankings take effect, and then not later than 30 calendar days after the last business day of each subsequent calendar quarter, the Secretary shall provide each servicer with an evaluation of their performance under such rules.

(2) No later than 45 calendar days after the last business day of the fourth calendar quarter during which the Secretary evaluates the performance of servicers, and then annually thereafter, VA shall advise each servicer of its tier ranking.

(3) Any entity which begins servicing guaranteed loans after the first calendar quarter occurring after rules for determining tier rankings take effect shall be presumed to be in tier two. The Secretary will evaluate the performance of such servicer as provided in paragraph (c)(1) of this section. The Secretary will advise such servicer of its tier ranking at the time other servicers are advised of their tier rankings pursuant to paragraph (c)(2) of this section, provided the servicer has received evaluations for at least four continuous calendar quarters.

(d) The quarterly evaluation and tier ranking of a servicer shall be deemed to be confidential and privileged and shall not be disclosed by the Secretary to any other party.

(Authority: 38 U.S.C. 3703(c))

§ 36.4819 Servicer loss-mitigation options and incentives.

(a) The Secretary will pay a servicer in tiers one, two, or three an incentive payment for each of the following successful loss-mitigation options or alternatives to foreclosure completed: repayment plans, special forbearance agreements, loan modifications, compromise sales, and deeds-in-lieu of foreclosure. Only one incentive payment will be made with respect to any default required to be reported to the Secretary pursuant to § 36.4817(c). No incentive payment will be made to a servicer in tier four. The options and alternatives are listed in paragraph (b) of this section from top to bottom in their preferred order of consideration (i.e., a hierarchy for review), but VA recognizes that individual circumstances may lead to ''out of the ordinary'' considerations.

(b) The amount of the incentive payment is as follows:

Tier ranking	One	Two	Three	Four
Repayment Plan	$200	$160	$120	$0
Special Forbearance	200	160	120	0
Loan Modification	700	500	300	0
Compromise Sale	1,000	800	600	0
Deed in Lieu of Foreclosure	350	250	150	0

(c) For purposes of this section, a loss-mitigation option or alternative to foreclosure will be deemed successfully completed as follows:

(1) With respect to a repayment plan (as defined in § 36.4801), when the loan reinstates;

(2) With respect to special forbearance (as defined in § 36.4801), when the loan reinstates. If a repayment plan is developed at the end of the forbearance period, then the special forbearance is not eligible for an incentive payment, although the subsequent repayment plan may be eligible upon loan reinstatement;

(3) With respect to a loan modification, when the modification is executed and the loan reinstates;

(4) With respect to a compromise sale, when the claim under guaranty is filed; or

(5) With respect to a deed-in-lieu of foreclosure, when the claim under guaranty is filed.

(d) Incentive payments with respect to repayment plans, special forbearances and loan modifications shall be made no less frequently than monthly. For all other successful loss-mitigation options, incentives shall be paid in the final claim payment.

(e) The Secretary shall reserve the right to stop an incentive payment to a servicer if the servicer fails to perform adequate servicing.

(Authority: 38 U.S.C. 3703(c), 3720, 3722)

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0021.)

§ 36.4820 Refunding of loans in default.

(a) Upon receiving a notice of default or a notice under § 36.4817, the Secretary may require the holder upon penalty of otherwise losing the guaranty or insurance to transfer and assign the loan and the security therefore 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 § 36.4828.

(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.

(c) Servicers must deliver to the Secretary all legal documents, including but not limited to proper loan assignments, required as evidence of proper loan transfer within 60 calendar days from the date that VA sends notice to the servicer that VA has decided to refund a loan under this section. Servicers exhibiting a continued failure to provide timely loan transfer documentation may, at the discretion of the Secretary and following advance notice to the servicer, be subject to temporary suspension of all property acquisition and claim payments until all deficiencies identified in the notice provided to the servicer have been corrected.

(Authority: 38 U.S.C. 3703(c) and 3732(a))

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0362.)

§ 36.4821 Service of process.

(a) In any legal or equitable proceeding to which the Secretary is a party (including probate and bankruptcy proceedings) arising from a loan guaranteed, insured, or made, or a property acquired by the Secretary pursuant to title 38, U.S.C. chapter 37, original process and any other process prior to appearance that may be served on the Secretary must be delivered to the VA Regional Counsel located in the jurisdiction in which the proceeding is docketed. Copies of such process will also be served on the Attorney General of the United States and the United States Attorney having jurisdiction over that area. 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. 3703(c) and 3720(a))

(b) 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. 3720, 3732)

§ 36.4822 Loan termination.

(a) For purposes of this part, a holder, using reasonable diligence must complete a foreclosure within the timeframe and in the manner determined by the Secretary. In determining what constitutes allowable time and method for foreclosure, the Secretary shall review allowances for time and method in connection with the foreclosure of single-family housing loans issued by HUD, Fannie Mae, and Freddie Mac, as well as State statutory requirements. The Secretary will review such timeframes annually and, as the Secretary deems necessary, publish in the **Federal Register** a table setting forth the timeframes and methods the Secretary determines to be reasonable. The schedule will reflect the timeframe allowed for the standard, acceptable method for foreclosure proceedings in each State. The use of another method will require prior approval from VA. VA will maintain the loan termination time allowable timeframes on a Web site under VA's control, such as at *http://www.homeloans.va.gov.*

(b)(1) At least 30 days prior to the scheduled or anticipated date of the liquidation sale, the holder must request that VA assign an appraiser to conduct a liquidation appraisal.

(2) If the holder (or its authorized servicing agent) has been approved by the Secretary to process liquidation appraisals under 38 CFR 36.4848, the appraiser shall forward the liquidation appraisal report directly to the holder for a determination of the fair market value of the property pursuant to § 36.4848.

(3) If the holder (or its authorized servicing agent) has not been approved by the Secretary to process liquidations appraisals under 38 CFR 36.4848, the Secretary shall review the appraisal and determine the fair market value of the property. The Secretary will provide the holder with a statement of the fair market value.

(4)(i) Except as provided in paragraph (b)(4)(ii) of this section, a liquidation appraisal or statement of fair market value issued pursuant to paragraph (b)(3) of this section will be valid for 180 calendar days.

(ii) The Secretary may specify in writing a shorter validity period, not less than 90 calendar days, for a liquidation appraisal or statement of fair market value if rapidly-changing market conditions in the area where the property is located make such shorter validity period in the best fiscal interests of the United States.

(c) Prior to the liquidation sale, the holder shall compute the net value of the property securing the guaranteed loan by subtracting the estimated costs to the Secretary for the acquisition and disposition of the property from the fair market value, as determined under paragraph (b) of this section. Those costs will be calculated using the percentage derived by the Secretary and published in the **Federal Register** pursuant to § 36.4801.

(d) If the holder learns of any material damage to the property occurring after the appraisal and prior to the liquidation sale, the impact of such damage on the fair market value must be determined in consultation with the fee appraiser, and the net value adjusted accordingly.

(e)(1) A holder may approve a compromise sale of the property securing the loan without the prior approval of the Secretary provided that:

(i) The holder has determined the loan is insoluble;

(ii) The credit to the indebtedness (consisting of the net proceeds from the compromise sale and any waiver of indebtedness by the holder) must equal or exceed the net value of the property securing the loan; and

(iii) The current owner of the property securing the loan will not receive any proceeds from the sale of the property.

(2) A holder may request advance approval from the Secretary for a compromise sale notwithstanding that all of the conditions specified in paragraph (e)(1) of this section cannot be met if the holder believes such compromise sale would be in the best interests of the veteran and the Secretary.

(f)(1) A holder may accept a deed voluntarily tendered by the current owner of the property securing the loan in lieu of conducting a foreclosure without the prior approval of the Secretary provided that:

(i) The holder has determined the loan is insoluble;

(ii) The holder has computed the net value of the property securing the loan pursuant to paragraph (c) of this section;

(iii) The holder has considered a compromise sale pursuant to paragraph (e) of this section and determined such compromise sale is not practical; and,

(iv) The holder has determined the current owner of the property can convey clear and marketable title to the property that would meet the standard stated in paragraph (d)(5) of § 36.4823.

(2) A holder may request advance approval from the Secretary for a deed-in-lieu of foreclosure notwithstanding that all of the conditions specified in paragraph (f)(1) of this section cannot be met if the holder believes such deed-in-lieu would be in the best interests of the veteran and the Secretary.

(Authority: 38 U.S.C. 3703(c), 3732)

§ 36.4823 Election to convey security.

(a) If the holder acquires the property that secured the guaranteed loan at the liquidation sale or through acceptance of a deed-in-lieu of foreclosure and if, under 38 U.S.C. 3732(c), the Secretary may accept conveyance of the property, the holder must notify the Secretary by electronic means no later than 15 calendar days after the date of liquidation sale (i.e., the event which fixes the rights of the parties in the property, such as the date of foreclosure sale, date of recordation of a deed-in-lieu of foreclosure, or confirmation/ratification of sale date when required under local practice) that the holder elects to convey the property to the Secretary. The Secretary will not accept conveyance of the property if the holder fails to notify the Secretary of its election within such 15 calendar days. In computing the eligible indebtedness under 38 U.S.C. 3732(c), the holder may follow the alternative procedure described in paragraph (b) of this section.

(b) If the calculation by the holder shows that the net value is equal to or less than the unguaranteed portion of the loan (i.e., the total indebtedness minus VA's maximum claim payable under the guaranty), this would preclude conveyance under 38 U.S.C. 3732(c). However, the holder may desire to convey the property to VA and may decide to waive a portion of the indebtedness to the extent that the property may be conveyed under 38 U.S.C. 3732(c). In such a case, the holder must provide the notice described in paragraph (a) of this section, and must subsequently waive that portion of the total indebtedness remaining after application of the net value amount and VA's guaranty claim payment. The holder must send the borrower(s) a notice describing the amount of indebtedness that has been waived no later than 15 calendar days after receipt of the guaranty claim.

(c) The holder, in accounting to the Secretary in connection with the conveyance of any property pursuant to 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 § 36.4814. 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 38 U.S.C. 3732(c):

(1) State and documentary stamp taxes as may be required.

(2) Amount expended for taxes, special assessments, including such payments which are specified in paragraph (d)(4) of this section.

(3) Recording fees.

(4) Any other expenditures in connection with the property which are approved by the Secretary, including, but not limited to, the cost of a title policy insuring title in the name of the Secretary of Veterans Affairs.

(d) The conveyance or transfer of any property to the Secretary pursuant to this section shall be subject to the following provisions:

(1) The notice of the holder's election to convey the property to the Secretary shall state the amount of the holder's successful bid 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. With respect to a voluntary conveyance to the holder in lieu of foreclosure, the amount of the holder's successful bid shall be deemed to be the lesser of the net value of the property or the total indebtedness.

(2) 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 request endorsements on all 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. If insurers cancel policies, holders must properly account for any unearned premiums refunded by the insurer.

(3) Occupancy of the property by anyone properly in possession by virtue of and during a period of redemption, or by anyone 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) The notice shall provide property tax information to include all taxing authority property identification numbers. Any taxes, special assessments or ground rents due and payable within 30 days after date of conveyance or transfer to the Secretary must be paid by the holder.

(5)(i) Each conveyance or transfer of real property to the Secretary pursuant to this section shall be acceptable if:

(A) 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

(B) 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.

(ii) Any title 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 § 36.4854(b), *Provided,* that:

(A) 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.

(B) 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 § 36.4827.

(iii) The acceptability of a conveyance or transfer pursuant to the requirements of this paragraph will generally be established by delivery to the Secretary of the following evidence of title showing that title to the property of the quality specified in this paragraph (d)(5) is or will be vested in the Secretary:

(A) A copy of the deed or document evidencing transfer of interest and title at the liquidation sale;

(B) A special warranty deed conveying the property to the Secretary;

(C) Origination Deed of Trust or Mortgage;

(D) Original or Copy of Mortgagee's Title Insurance Policy from Loan Origination (except in Iowa, where a title abstract is required);

(E) Owner's Title Insurance Policy issued after loan termination in the name of the Secretary (except in Iowa, where a title abstract is required);

(F) Loan Assignments;

(G) Appointment of Substitute Trustee (where required as part of the termination process);

(H) Estoppel Affidavit for deed in lieu of foreclosure, if required by State law and appropriate language cannot be included in the deed in lieu of foreclosure; and/or

(I) Any evidence that the Secretary may reasonably require.

(iv) In lieu of such title evidence listed in paragraph (d)(5)(iii) of this section, 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.

(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. 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 (d)(11) 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 of the holder's election to convey or transfer the property 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 conveyance should be made to ''Secretary of Veterans Affairs, an Officer of the United States.'' The name of the incumbent Secretary should not be included unless State law requires naming a real person.

(9) 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. The holder shall be liable to the Secretary for all penalties and interest associated with taxes not timely paid by the holder prior to conveyance.

(10) 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.

(11) 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.

(e) Except as provided in paragraph (d)(6) of this section, the provisions of this section shall not be in derogation of any rights which the Secretary may have under § 36.4828. The Under Secretary for Benefits, 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.

(Authority: 38 U.S.C. 3720, 3732)

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0381.)

§ 36.4824 Guaranty claims; subsequent accounting.

(a) Subject to the limitation that the total amounts payable shall in no event exceed the amount originally guaranteed, or in the case of a modified loan, such amount as may have been increased under the provisions of § 36.4815(h)(2), the amount payable on a claim for the guaranty shall be the percentage of the loan originally guaranteed, or the percentage as adjusted under § 36. 4815(h)(2), whichever is applicable, applied to the sum of:

(1) The unpaid principal as of the date of the liquidation sale;

(2) Allowable expenses/advances as described in § 36.4814; and

(3) The lesser of:

(i) The unpaid interest as of the date of the liquidation sale; or

(ii) The unpaid interest for the reasonable period that the Secretary has determined, pursuant to § 36.4822(a), it should have taken to complete the foreclosure, plus 210 days from the due date of the last paid installment. This amount will be increased if the Secretary determines the holder was unable to complete the foreclosure within the time specified in this paragraph due to Bankruptcy proceedings, appeal of the foreclosure by the debtor, the holder granting forbearance in excess of 30 days at the request of the Secretary, or other factors beyond the control of the holder.

(b) Deposits or other credits or setoffs legally applicable to the indebtedness 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.

(c)(1) Credits accruing from the proceeds of a liquidation sale shall be reported to the Secretary incident to claim submission, and the amount payable on the claim shall in no event exceed the remaining balance of the indebtedness.

(2) The amount payable under the guaranty shall be computed applying the formulae in 38 U.S.C. 3732(c). With respect to a voluntary conveyance to the holder in lieu of foreclosure, the holder shall be deemed to have acquired the property at the liquidation sale for the lesser of the net value of the property or the total indebtedness.

(d)(1)(i) Except as provided in paragraph (d)(1)(ii) of this section, holders shall file a claim for payment under the guaranty electronically no later than 1 year after the completion of the liquidation sale. For purposes of this section, the liquidation sale will be considered completed when:

(A) The last act required under State law is taken to make the liquidation sale final, but excluding any redemption period permitted under State law;

(B) If a holder accepts a voluntary conveyance of the property in lieu of foreclosure, the date of recordation of the deed to the holder or the holder's designee; or

(C) In the case of a sale of the property to a third party for an amount less than is sufficient to repay the unpaid balance on the loan where the holder has agreed in advance to release the lien in exchange for the proceeds of such sale, the date of settlement of such sale.

(ii) With respect to any liquidation sale completed prior to February 1, 2008, all claims must be submitted no later than February 2, 2009.

(2) If additional information becomes known to a holder after the filing of a guaranty claim, the holder may file a supplemental claim provided that such supplemental claim is filed within the time period specified in paragraph (d)(1) of this section.

(3) No claim under a guaranty shall be payable unless it is submitted within the time period specified in paragraph (d)(1) of this section.

(4) A claim shall be submitted to VA electronically on the VA Loan Electronic Reporting Interface system.

(5) Supporting documents will not be submitted with the claim, but must be retained by the servicer and are subject to inspection as provided in § 36.4833 of this title.

(e) In the event that VA does not approve payment of any item submitted under a guaranty claim, VA shall notify the holder electronically what items are being denied and the reasons for such denial. The holder may, within 30 days after the date of such denial notification, submit an electronic request to VA that one or more items that were denied be reconsidered. The holder must present any additional information justifying payment of items denied.

(Authority: 38 U.S.C. 3703(c), 3720, 3732)

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0362.)

§ 36.4825 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 § 36.4820(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.

(Authority: 38 U.S.C. 3703(c), 3720, 3732)

§ 36.4826 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. Before a liquidation sale, an official authorized to act for the Secretary under provisions of § 36.4845 may approve a complete or 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 as follows:

(1) *Complete release.* VA will approve a complete release if an official authorized to act for the Secretary under § 36.4845 determines that all of the following are true:

(i) The loan default was caused by circumstances beyond the control of the obligor; and

(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; and

(iii) The obligor cooperated with VA in exploring all realistic alternatives to termination of the loan through foreclosure, and, either:

(A) 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 after the liquidation sale and still provide the necessities of life for himself or herself and his or her family; or,

(B) 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; or

(C) The obligor being released is not the current titleholder to the property and there are no indications of fraud, misrepresentation, or bad faith on the obligor's part in disposing of the property.

(2) *Partial release.* In the event of a partial release, 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. VA may authorize a partial release if an official authorized to act for the Secretary under § 36.4845 determines that all of the following are true:

(i) The loan default was caused by circumstances beyond the control of the obligor; and,

(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; and,

(iii) The obligor cooperated with VA in exploring all realistic alternatives to termination of the loan through foreclosure; and,

(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) *Review of obligor's financial situation.* For purposes of authorizing a complete or partial release under this paragraph, a VA official reviewing an obligor's financial situation will consider all of the following:

(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.

(4) Determinations made under paragraphs (e)(1) and (2) 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 uncollectible 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, 3703(c)(1), 5302)

(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 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)(1) 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:

(i) The proposed purchaser is creditworthy;

(ii) 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

(iii) The payments on the loan are current.

(2) 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.

(i) If a veteran requests a release of liability under paragraph (f) of this section, or if a borrower requests a release of liability pursuant to § 36.4809(c)(1)(vii), a holder described in the first sentence of § 36.4803(l)(1)(i) is authorized to and must make all decisions regarding the credit-worthiness of the transferee, subject to the right of a transferee to appeal any denial to the Secretary within 30 days of being notified in writing of the denial by the holder or servicer. The procedures and fees specified in §§ 36.4803(l)(1)(i) and 36.4813(d)(8) applicable to decisions under 38 U.S.C. 3714 shall also apply to decisions specified in this paragraph.

(Authority: 38 U.S.C. 3703(c), 3713 and 3714)

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0112.)

§ 36.4827 Release of security.

(a)(1) Except upon full payment of the indebtedness, or except as provided in paragraph (a)(2) of this section or in paragraphs (e) and (f) of § 36.4822, 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 prior approval of the Secretary.

(2) The holder may, without the prior approval of the Secretary, release the lien on a portion of the property securing the loan provided:

(i) The holder has obtained an appraisal from the Secretary showing the value of the security prior to the partial release of the lien and the value of the security on which the lien will remain;

(ii) The portion of the property still subject to the lien is fit for dwelling purposes; and

(iii) The loan-to-value ratio after the partial release of the lien:

(A) Will be not more than 80 percent; or

(B) If the loan-to-value ratio after the partial release of the lien is 80 percent or higher, any proceeds received as consideration from the partial release of the lien shall be applied to the unpaid loan balance.

(b) A holder may release from the lien personal property including crops without the prior approval of the Secretary.

(c) 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.

(d) 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 § 36.4817 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 § 36.4815; 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)

§ 36.4828 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.

(1) 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.

(2) [Reserved]

(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 § 36.4854(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, then 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. Adjustments under this section may be made for failure to comply with:

(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 (§ 36.4830),

(3) The procurement and maintenance of insurance coverage (§ 36.4829),

(4) Any notice required by § 36.4817,

(5) The release, conveyance, substitution, or exchange of security (§ 36.4827),

(6) Lack of legal capacity of a party to the transaction incident to which the guaranty or the insurance is granted (§ 36.4831),

(7) Failure of the lender to see that any escrowed or earmarked account is expended in accordance with the agreement,

(8) The taking into consideration of limitations upon the quantum or quality of the estate or property (§ 36.4854(b)),

(9) 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,

(c) If after the payment of a guaranty or an insurance loss, or after a loan is transferred pursuant to § 36.4820(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.

(Authority: 38 U.S.C. 3703 and 3720)

§ 36.4829 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. All moneys received under such policies covering payment of insured losses shall be applied to restoration of the security or to the loan balance. Flood insurance will be required on any building or personal property securing a loan at any time during the term of the loan that such security is located in an area identified by the Federal Emergency Management Agency as having special flood hazards and in which flood insurance has been made available under the National Flood Insurance Act, as amended. The amount of flood insurance must be at least equal to the lesser of the outstanding principal balance of the loan or the maximum limit of coverage available for the particular type of property under the National Flood Insurance Act, as amended. The Secretary cannot guarantee a loan for the acquisition or construction of property located in an area identified by the Federal Emergency Management Agency as having special flood hazards unless the community in which such area is situated is then participating in the National Flood Insurance Program.

(Authority: 38 U.S.C. 3703(c)(1), 42 U.S.C. 4106(a))

§ 36.4830 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4831 Capacity of parties to contract.

Nothing in §§ 36.4800 through 36.4880 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4832 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4833 Maintenance of records.

(a)(1) The holder shall maintain a record of the amounts of payments received on the obligation and disbursements chargeable thereto and the dates thereof, including copies of bills and receipts for such disbursements. These records shall be maintained until the Secretary ceases to be liable as guarantor or insurer of the loan, or, if the Secretary has paid a claim on the guaranty, until 3 years after such claim was paid. For the purpose of any accounting with the Secretary or computation of a claim, any holder who fails to maintain such record and, upon request, make it available to the Secretary for review 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, or to have not made the disbursement for which reimbursement is claimed, and the burden of going forward with evidence and of ultimate proof of the contrary shall be on such holder.

(2) The holder shall maintain records supporting their decision to approve any loss mitigation option for which an incentive is paid in accordance with § 36.4819(a). Such records shall be retained a minimum of 3 years from the date of such incentive payment and shall include, but not be limited to, credit reports, verifications of income, employment, assets, liabilities, and other factors affecting the obligor's credit worthiness, work sheets, and other documents supporting the holder's decision.

(3) For any loan where the claim on the guaranty was paid on or after February 1, 2008, or action described in paragraph (a)(2) of this section was taken after February 1, 2008, holders shall submit any documents described in paragraph (a)(1) or (a)(2) of this section to the Secretary in electronic form; i.e., an image of the original document in .jpg, .gif, .pdf, or a similar widely accepted format.

(b) The lender shall retain copies of all loan origination records on a VA-guaranteed loan for at least two years 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, 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 lender or holder pertaining to loans guaranteed or insured by the Secretary.

(Authority: 38 U.S.C. 3703(c)(1))

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0515.)

§ 36.4835 Delivery of notice.

Except where otherwise specified in this part, any notice required by §§ 36.4800 to 36.4880 to be given the Secretary must be in writing or such other communications medium as may be approved by an official designated in § 36.4845 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 §§ 36.4800 to 36.4880.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4836 [Reserved]

§ 36.4837 Conformance of loan instruments.

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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4838 Supplementary administrative action.

(a) Notwithstanding any requirement, condition, or limitation stated in or imposed by the regulations concerning the guaranty or insurance of loans to veterans, the Under Secretary for Benefits, 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 § 36.4845 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:

(1) The requirement in § 36.4808(a) that a lender obtain in 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);

(2) The requirements in § 36.4803(l) concerning the giving of notice in assumption cases under 38 U.S.C. 3714;

(3) The requirement in § 36.4824(d)(3) that no claim is payable unless it is submitted within 1 year after the liquidation sale;

(4) The requirement in § 36.4823(a) to submit notice of election to convey a property to VA within 15 days of the date of liquidation sale;

(5) The determination by the holder in § 36.4823(b) of the amount of indebtedness that must be waived in order to make a property eligible for conveyance;

(6) The determination in § 36.4814(f)(2) of the date beyond which no additional fees or charges will be allowed;

(7) The determination in § 36.4824(a)(3) of the interest payable on a claim under guaranty; and

(8) The reconsideration in § 36.4824(e) of the holder's electronic request for review of any denied items within the claim;

(b) Authority is hereby granted to the Loan Guaranty Officer to redelegate authority to make any determinations under this section.

(Authority: 38 U.S.C. 3714 and 3720)

§ 36.4839 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 all of the following conditions are met:

(1) The proceeds of such loan have been used to pay for the property purchased, constructed, repaired, refinanced, altered, or improved.

(2) Except as to refinancing loans pursuant to 38 U.S.C. 3710(a)(8), (a)(9)(B)(i), (a)(11), or (b)(7) and energy efficient mortgages pursuant to 38 U.S.C. 3710(d), 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. 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.

(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) A loan guaranteed under 38 U.S.C. 3710(d) which includes the cost of energy efficient improvements may exceed the reasonable value of the property. The cost of the energy efficient improvements that may be financed may not exceed $3,000; provided, however, that up to $6,000 in energy efficient improvements may be financed if the increase in the monthly payment for principal and interest does not exceed the likely reduction in monthly utility costs resulting from the energy efficient improvements.

(Authority: 38 U.S.C. 3710)

(c) 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 § 36.4823, and all accounting), 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. 3703(c)(1), 3710, 3712)

§ 36.4840 Underwriting standards, processing procedures, lender responsibility, and lender certification.

(a) *Use of standards.* The standards contained in paragraphs (c) through (j) of this section will be used to determine whether the veteran's present and anticipated income and expenses, and credit history are satisfactory. These standards do not apply to loans guaranteed pursuant to 38 U.S.C. 3710(a)(8) except for cases where the Secretary is required to approve the loan in advance under § 36.4807.

(Authority: 38 U.S.C. 3703, 3710)

(b) *Waiver of standards.* Use of the standards in paragraphs (c) through (j) of this section for underwriting home loans will be waived only in extraordinary circumstances when the Secretary determines, considering the totality of circumstances, that the veteran is a satisfactory credit risk.

(c) *Methods.* The two primary underwriting standards that will be used in determining the adequacy of the veteran's present and anticipated income are debt-to-income ratio and residual income analysis. They are described in paragraphs (d) through (f) of this section. Ordinarily, 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 exceptions shall apply to cases where a veteran does not meet both standards:

(1) If the debt-to-income ratio is 41 percent or 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 (c)(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 (c)(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 are not required.

(4) In any case described by paragraphs (c)(1) and (c)(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 paragraph (c)(5) of this section, justifying the approval 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 that 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 the criteria set forth in paragraph (g) 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;

(xi) Low debt-to-income ratio;

(xii) Tax credits of a continuing nature, such as tax credits for child care; and

(xiii) Tax benefits of home ownership.

(6) The list in paragraph (c)(5) of this section is not exhaustive and the items are not in any priority order. Valid compensating factors should represent unusual strengths rather than mere satisfaction of basic program requirements. Compensating factors must be relevant to the marginality or weakness.

(d) *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) of 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; e.g., 35.6 percent would be rounded to 36 percent. The standard is 41 percent or less. If the ratio is greater than 41 percent, the steps cited in paragraphs (c)(1) through (c)(6) of this section apply.

(e) *Residual income guidelines.* The guidelines provided in this paragraph 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. All members of the household must be included in determining if the residual income is sufficient. They must be counted even if the veteran's spouse is not joining in title or on the note, or if there are any other individuals depending on the veteran for support, such as children from a spouse's prior marriage who are not the veteran's legal dependents. It is appropriate, however, to reduce the number of members of a household to be counted for residual income purposes if there is sufficient verified income not otherwise included in the loan analysis, such as child support being regularly received as discussed in paragraph (e)(4) of this section. In the case of a spouse not to be obligated on the note, verification that he/she has stable and reliable employment as discussed in paragraph (f)(3) of this section would allow not counting the spouse in determining the sufficiency of the residual income. 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 $79,999 and for loan amounts of $80,000 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 require closer scrutiny. In such cases, consideration should be given to the ability of the borrower and spouse to accumulate liquid assets, such as cash and bonds, and to the amount of debts incurred while paying a lesser amount for shelter. For example, if an application indicates 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 (c) through (j) of this section. The residual income guidelines are as follows:

(1) *Table of residual incomes by region (for loan amounts of $79,999 and below):*

TABLE OF RESIDUAL INCOMES BY REGION

[For loan amounts of $79,999 and below]

Family size [1]	Northeast	Midwest	South	West
1	390	382	382	425
2	654	641	641	713
3	788	772	772	859
4	888	868	868	967
5	921	902	902	1,004

[1] For families with more than five members, add $75 for each additional member up to a family of seven. ''Family'' includes all members of the household.

(2) *Table of residual incomes by region (for loan amounts of $80,000 and above):*

TABLE OF RESIDUAL INCOMES BY REGION

[For loan amounts of $80,000 and above]

Family size [1]	Northeast	Midwest	South	West
1	450	441	441	491
2	755	738	738	823
3	909	889	889	990
4	1,025	1,003	1,003	1,117
5	1,062	1,039	1,039	1,158

[1] For families with more than five members, add $80 for each additional member up to a family of seven. ''Family'' includes all members of the household.

(3) *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, West Virginia; West—Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington and Wyoming.

(4) *Military adjustments.* For loan applications involving an active-duty servicemember or military retiree, 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 paragraph (e) of this section.)

(f) *Stability and reliability of 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.

(1) *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 (12 CFR part 202), 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 (f)(4) 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 considered 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 and pay stubs must be no more than 120 days (180 days for new construction) old to be considered valid. For loans closed automatically, this requirement will be considered satisfied if the date of the employment verification is within 120 days (180 days for new construction) of the date the note is signed. For prior approval loans, this requirement will be considered satisfied if the verification of employment is dated within 120 days of the date the application is received by VA.

(2) *Active-duty, Reserve, or National Guard applicants.* (i) In the case of an active-duty applicant, a military Leave & Earnings Statement is required and will be used instead of an employment verification. The statement must be no more than 120 days old (180 days for new construction) and must be the

original or a lender-certified copy of the original. For loans closed automatically, this requirement is satisfied if the date of the Leave & Earnings Statement is within 120 days (180 days for new construction) of the date the note is signed. For prior approval loans, this requirement will be considered satisfied if the verification of employment is dated within 120 days of the date the application is received by VA.

(ii) For servicemembers within 12 months of release from active duty, or members of the Reserves or National Guard within 12 months of release, one of the following is also required:

(A) Documentation that the servicemember has in fact already reenlisted or extended his/her period of active duty or Reserve or National Guard service to a date beyond the 12-month period following the projected closing of the loan.

(B) Verification of a valid offer of local civilian employment following release from active duty. All data pertinent to sound underwriting procedures (date employment will begin, earnings, etc.) must be included.

(C) A statement from the servicemember that he/she intends to reenlist or extend his/her period of active duty or Reserve or National Guard service to a date beyond the 12 month period following the projected loan closing date, and a statement from the servicemember's commanding officer confirming that the servicemember is eligible to reenlist or extend his/her active duty or Reserve or National Guard service as indicated and that the commanding officer has no reason to believe that such reenlistment or extension will not be granted.

(D) Other unusually strong positive underwriting factors, such as a down payment of at least 10 percent, significant cash reserves, or clear evidence of strong ties to the community coupled with a nonmilitary spouse's income so high that only minimal income from the active duty servicemember or member of the Reserves or National Guard is needed to qualify.

(iii) Each active-duty member who applies for a loan must be counseled through the use of VA Form 26–0592, Counseling Checklist for Military Homebuyers. Lenders must submit a signed and dated VA Form 26–0592 with each prior approval loan application or automatic loan report involving a borrower on active duty.

(3) *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. If an employer puts N/A or otherwise declines to complete a verification of employment statement regarding the probability of continued employment, no further action is required of the lender. Reliability will be determined based on the duration of the borrower's current employment together with his or her overall documented employment history. 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. Generally, the reliability of such income cannot be demonstrated unless the income has continued for 2 years. 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 for at least 12 months, be used to offset the payments due on debts and obligations of an intermediate term, i.e., 6 to 24 months. 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 intermediate-term debts, as described in this paragraph. Also, the likely duration of certain military allowances cannot be determined and, therefore, will be used only to offset intermediate-term debts, as described in this paragraph. 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 beyond 12 months. The total period of active and reserve service may be helpful in this regard. Otherwise, such income may be used to offset intermediate-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 for a loan if it can be determined that the income will probably continue for 3 years or more.

(4) *Tax-exempt income*. Special consideration can be given to verified nontaxable income once it has been established that such income is likely to continue (and remain untaxed) into the foreseeable future. Such income includes certain military allowances, child support payments, workers' compensation benefits, disability retirement payments and certain types of public assistance payments. In such cases, current income tax tables may be used to determine an amount which can be prudently employed to adjust the borrower's actual income. This adjusted or ''grossed up'' income may be used to calculate the monthly debt-to-income ratio, provided the analysis is documented. Only the borrower's actual income may be used to calculate the residual income. Care should be exercised to ensure that the income is in fact tax-exempt.

(5) *Alimony, child support, maintenance, workers' compensation, foster care payments*. (i) 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 (12 CFR part 202)), such payments are considered as income to the extent that the payments are likely to be consistently 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 the 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. 1681(b)) 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.

(ii) If the applicant chooses to reveal income related to workers' compensation, it will be considered as income to the extent it can be determined such income will continue.

(iii) Income received specifically for the care of any foster child(ren) may be counted as income if documented. Generally, however, such foster care income is to be used only to balance the expenses of caring for the foster child(ren) against any increased residual income requirements.

(6) *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 to utilize available on-base housing when possible. In order for a quarters allowance 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. A Department of Defense form, DD Form 1747, Status of Housing Availability, is used by the Family Housing Office to advise personnel regarding family housing. The applicant's quarters allowance cannot be considered unless item b (Permanent) or d is completed on DD Form 1747, dated October 1990. 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 on-base housing are so long that it 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.

(7) *Automobile (or similar) allowance*. Generally, automobile allowances are paid to cover specific expenses related to an applicant's employment, and it is appropriate to use such income to offset a corresponding car payment. However, in some instances, such an allowance may exceed the car payment. With proper documentation, income from a car allowance which exceeds the car payment can be counted as effective income. Likewise, any other similar type of allowance which exceeds the specific expense involved may be added to gross income to the extent it is documented to exceed the actual expense.

(8) *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. Lenders should also obtain signed and dated individual income tax returns, plus applicable schedules, for the previous 2 years, or for whatever additional period is deemed necessary to properly demonstrate a satisfactory earnings record. The length of the veteran's employment in the type of occupation for which commissions are paid 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. Generally, income from commissions is considered stable when the applicant has been receiving such income for at least 2 years. Less than 2 years of income from commissions cannot usually be considered stable. When an applicant has received income from commissions for less than 1 year, it will rarely be possible to demonstrate that the income is stable for qualifying purposes; such cases would require in-depth development.

(9) *Self-employment*. Generally, income from self-employment is considered stable when the applicant has been in business for at least 2 years. Less than 2 years of income from self-employment cannot usually be considered stable unless the applicant has had previous related employment and/or extensive specialized training. When an applicant has been self-employed less than 1 year, it will rarely be possible to demonstrate that the income is stable for qualifying purposes; such cases would require in-depth development. The following documentation is required for all self-employed borrowers:

(i) 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 balance sheet based on the financial records. The financial statement must be sufficient for a loan underwriter to determine the necessary information for loan approval and an independent audit (on the veteran and/or the business) by a Certified Public Accountant will be required if necessary for such determination; and

(ii) Copies of signed individual income tax returns, plus all applicable schedules for the previous 2 years, or for whatever additional period is deemed necessary to properly demonstrate a satisfactory earnings record, must be obtained. If the business is a corporation or partnership, copies of signed Federal business income tax returns for the previous two years plus all applicable schedules for the corporation or partnership must be obtained; and

(iii) 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, explanation 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.

(10) *Recently discharged veterans*. Loan applications received from

recently discharged veterans who have little or no employment experience other than their 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.

(i) 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.

(ii) 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 an 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.

(iii) 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. This 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 qualify 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.

(iv) To illustrate the provisions of paragraph (f)(10), 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 nonqualifying 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.

(11) *Employment of short duration*. The provisions of paragraph (f)(7) 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 than 1 year as well as signed and dated 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 earnings record. 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.

(12) *Rental income*—(i) *Multi-unit subject property*. When the loan pertains to a structure with more than 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 of any 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 75 percent of the amount indicated on the lease or rental agreement, unless a greater percentage can be documented.

(ii) *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.

(iii) *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 (f)(7) 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.

(13) *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 (f)(14) 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.

(14) *Mortgage credit certificates.* (i) The Internal Revenue Code (26 U.S.C.) 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 MCCs. Veterans who are recipients of MCCs 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.

(ii) 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.

(iii) For credit underwriting purposes, the amount of tax credit allowed to a veteran under an 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 percent × $600) tax credit each month. However, because the annual tax credit, which amounts to $2,160 (12 × $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 by the amount of the tax credit to $433 ($600 − $167). This reduction should also be reflected when calculating Federal income tax.

(iv) For underwriting purposes, the amount of the tax credit is limited to the amount of the veteran's maximum tax liability. If, in the example in paragraph (f)(14)(iii) of this section, the veteran's tax liability for the year were only $1,500, the monthly tax credit would be limited to $125 ($1,500/12).

(g) *Credit.* The conclusion reached as to whether or not the veteran and spouse are satisfactory credit risks must also be based on a careful analysis of the available credit data. Regulation B (12 CFR part 202), promulgated by the Federal Reserve Board pursuant to the Equal Credit Opportunity Act, requires that lenders, in evaluating creditworthiness, shall consider, on the applicant's request, the credit history, when available, of any account reported in the name of the applicant's spouse or former spouse which the applicant can demonstrate accurately reflects the applicant's creditworthiness. In other than community property states, if the spouse will not be contractually obligated on the loan, Regulation B prohibits any request for or consideration of information about the spouse concerning income, employment, assets or liabilities. In community property states, information concerning a spouse may be requested and considered in the same manner as that for the applicant.

(1) *Adverse data.* If the analysis develops any derogatory credit information and, despite such facts, it is determined that the veteran and spouse are satisfactory credit risks, the basis for the decision must be explained. If a veteran 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. Such defenses are not applicable when the debt has been reduced to judgment. Where a collection account has been established, if it is determined that the borrower is a satisfactory credit risk, it is not mandatory that such an account be paid off in order for a loan to be approved. Court-ordered judgments, however, must be paid off before a new loan is approved.

(2) *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 one to two 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 credit subsequent to the bankruptcy and has met the credit payments in a satisfactory manner over a continued period; and

(ii) The bankruptcy was caused by circumstances beyond the control of the borrower or spouse, e.g., unemployment, prolonged strikes, medical bills not covered by insurance. Divorce is not generally viewed as beyond the control of the borrower and/or spouse. 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 risk may be made provided there is no derogatory credit information prior to self-employment, there is no derogatory credit information subsequent to the bankruptcy, and the failure of the business was not due to misconduct. If a borrower or spouse has been discharged in bankruptcy within the past 12 months, it will not generally be possible to determine that the borrower or spouse is a satisfactory credit risk.

(3) *Petition under Chapter 13 of Bankruptcy Code.* A petition under chapter 13 of the Bankruptcy Code (11 U.S.C.) 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 12 months' worth of payments have been made satisfactorily and the Trustee or Bankruptcy Judge approves of the new credit.

(4) *Foreclosures.* (i) When the credit information shows that the veteran or spouse has had a foreclosure on a prior mortgage; e.g., a VA-guaranteed or HUD-insured mortgage, this will not in itself disqualify the borrower from obtaining the loan. Lenders and field station personnel should refer to the preceding guidelines on bankruptcies for cases

involving foreclosures. As with a borrower who has been adjudicated bankrupt, it is necessary to develop complete information as to the facts and circumstances of the foreclosure.

(ii) When VA pays a claim on a VA-guaranteed loan as a result of a foreclosure, the original veteran may be required to repay any loss to the Government. In some instances VA may waive the veteran's debt, in part or totally, based on the facts and circumstances of the case. However, guaranty entitlement cannot be restored unless the Government's loss has been repaid in full, regardless of whether or not the debt has been waived, compromised, or discharged in bankruptcy. Therefore, a veteran who is seeking a new VA loan after having experienced a foreclosure on a prior VA loan will in most cases have only remaining entitlement to apply to the new loan. The lender should assure that the veteran has sufficient entitlement for its secondary marketing purposes.

(5) *Federal debts.* An applicant for a Federally-assisted loan will not be considered a satisfactory credit risk for such loan if the applicant is presently delinquent or in default on any debt to the Federal Government, e.g., a Small Business Administration loan, a U.S. Guaranteed Student loan, a debt to the Public Health Service, or where there is a judgment lien against the applicant's property for a debt owed to the Government. The applicant may not be approved for the loan until the delinquent account has been brought current or satisfactory arrangements have been made between the borrower and the Federal agency owed, or the judgment is paid or otherwise satisfied. Of course, the applicant must also be able to otherwise qualify for the loan from an income and remaining credit standpoint. Refinancing under VA's interest rate reduction refinancing provisions, however, is allowed even if the borrower is delinquent on the VA guaranteed mortgage being refinanced. Prior approval processing is required in such cases.

(6) *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 that occurred over 3 years ago.

(7) *Consumer credit counseling plan.* If a veteran, or veteran and spouse, have prior adverse credit and are participating in a Consumer Credit Counseling plan, they may be determined to be a satisfactory credit risk if they demonstrate 12 months' satisfactory payments and the counseling agency approves the new credit. If a veteran, or veteran and spouse, have good prior credit and are participating in a Consumer Credit Counseling plan, such participation is to be considered a neutral factor, or even a positive factor, in determining creditworthiness.

(8) *Re-establishment of satisfactory credit.* In circumstances not involving bankruptcy, satisfactory credit is generally considered to be reestablished after the veteran, or veteran and spouse, have made satisfactory payments for 12 months after the date of the last derogatory credit item.

(9) *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., 10 months or over. Other accounts for terms of less than 10 months must, of course, be considered in determining ability to meet family expenses. Certainly, any severe impact on the family's resources for any period of time must be considered in the loan analysis. For example, monthly payments of $300 on an auto loan with a remaining balance of $1,500 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 $300 payments for the first, most critical months of the home loan.

(10) *Requirements for verification.* 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 dated. 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 120 days old (180 days for new construction) 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 120 days (180 days for new construction) of the date the note is signed. For prior approval loans, this requirement will be considered satisfied if the date of the credit report or verification is within 120 days of the date the application is received by VA. Of major significance are the applicant's rental history and outstanding or recently retired mortgages, if any, particularly prior VA loans. Lenders should be sure ratings on such accounts are obtained; a written explanation is required when ratings are not available. 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. When a pay stub or leave-and-earnings statement indicates an allotment, the lender must investigate the nature of the allotment(s) to determine whether the allotment is related to a debt. Debts assigned to an ex-spouse by a divorce decree will not generally be charged against a veteran-borrower.

(11) *Job-related expenses.* Known job-related expenses should be documented. This will include costs for any dependent care, 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.

(12) *Credit reports.* Credit reports obtained by lenders on VA-guaranteed loan applications must be either a three-file Merged Credit Report (MCR) or a Residential Mortgage Credit Report (RMCR). If used, the RMCR must meet the 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. All credit reports obtained by the lender must be submitted to VA.

(h) *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 (see § 36.4839(a)(3)) 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.) Verifications must be no more than 120 days old (180 days for new construction) 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 120 days (180 days for new construction) of the date of the veteran's application to the lender. For prior approval loans, this requirement will be considered satisfied if the verification of employment is dated within 120 days of the date the application is received by VA. 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.

(i) *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.

(j) *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 (j)(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 (j)(3) and (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.

(k) *Lender certification.* Lenders 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 this section.

(1) *Definitions.* The definitions contained in part 42 of this chapter and the following definitions are applicable in this section.

(i) *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:

(A) The materiality and importance of the false certification to the determination to issue the guaranty or to approve the assumption;

(B) The frequency and past pattern of such false certifications by the lender; and

(C) Any exculpatory or mitigating circumstances.

(ii) *Complaint.* Complaint includes the assessment of liability served pursuant to this section.

(iii) *Defendant.* Defendant means a lender named in the complaint.

(iv) *Lender.* Lender includes the holder approving loan assumptions pursuant to 38 U.S.C. 3714.

(2) *Procedures for certification.* (i) As a condition to VA issuance of a loan guaranty on all loans closed on or after October 27, 1994, and as a prerequisite to an effective loan assumption on all loans assumed pursuant to 38 U.S.C. 3714 on or after November 17, 1997, 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 chapter 37 of title 38 United States Code 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.

(ii) The certification shall be executed by an officer of the lender authorized to execute documents and act on behalf of the lender.

(3) *Penalty.* Any lender who knowingly and willfully makes a false certification required pursuant to § 36.4840(k)(2) shall be liable to the United States 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.

(l) *Assessment of liability.* (1) Upon an assessment confirmed by the Under Secretary for Benefits, in consultation with the Investigating Official, that a certification, as required in this section, is false, a report of findings of the Under Secretary for Benefits 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 Under Secretary for Benefits and the 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.

(m) *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.

(n) *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 2 CFR parts 180 and 801 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. 3703(c)(1), 3710(g))

(The Office of Management and Budget has approved the information collection requirements of this section under control number 2900–0521.)

§ 36.4841 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; or

(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.

(Authority 38 U.S.C. 3703(c)(1), 3720)

§ 36.4842 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.

(Authority 38 U.S.C. 3703(c)(1), 3731)

§ 36.4843 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.

(Authority 38 U.S.C. 3703(c)(1), 3731)

§ 36.4845 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) through (6) 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)(1) Designated positions are as follows:

(i) Under Secretary for Benefits.

(ii) Director, Loan Guaranty Service.

(iii) Director, Medical and Regional Office Center.

(iv) Director, VA Regional Office and Insurance Center.

(v) Director, Regional Office.

(vi) Loan Guaranty Officer.

(vii) Assistant Loan Guaranty Officer.

(2) The authority hereby delegated to employees of the positions designated in paragraph (b)(1) of this section may, with the approval of the Under Secretary for Benefits, 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 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 Under Secretary for Benefits, or the Director, Loan Guaranty Service, under §§ 36.4823(e), 36.4838 or 36.4846, *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.

(e)(1) Authority is hereby delegated to the officers, designated in paragraph (e)(2) of this section, of the entity performing loan servicing functions under a contract with the Secretary to execute on behalf of the Secretary all documents necessary for the servicing and termination of a loan made or acquired by the Secretary pursuant to 38 U.S.C. chapter 37 (other than under subchapter vi of that chapter). Documents executed under this paragraph include but are not limited to: Loan modification agreements, notices of default and other documents necessary for loan foreclosure or termination, notices of appointment or substitution of trustees under mortgages or deeds of trust, releases or satisfactions of mortgages or deeds of trust, acceptance of deeds-in-lieu of foreclosure, loan assumption agreements, loan assignments, deeds tendered upon satisfaction or conversion of an installment land sales contract, and documents related to filing, pursuing and settling claims with insurance companies relating to hazard coverage on properties securing loans being serviced.

(2) The designated officers are:

(i) Vice President;

(ii) Assistant Vice President; and

(iii) Assistant Secretary.

(3) The Director, Loan Guaranty Service, Washington, DC, shall maintain a log listing all persons authorized to execute documents pursuant to paragraph (e) of this section and the dates such persons held such authority, together with certified copies of resolutions of the board of directors of the entity authorizing such individuals to perform the functions specified in paragraph (e)(1) of this section. These records shall be available for public inspection and copying at the Office of the Director of VA Loan Guaranty Service, Washington, DC 20420.

(f)(1) Authority is hereby delegated to the officers, designated in paragraph (f)(2) of this section, of the entity performing property management and sales functions under a contract with the Secretary to execute on behalf of the Secretary all documents necessary for the management and sales of residential real property acquired by the Secretary pursuant to 38 U.S.C. chapter 37. Documents executed under this paragraph include but are not limited to: Sales contracts, deeds, documents relating to removing adverse occupants, and any documents relating to sales closings. The authorization to execute deeds is limited to deeds other than general warranty deeds.

(2) The designated officers are:

(i) Senior Vice President;

(ii) Vice President;

(iii) Assistant Vice President;

(iv) Assistant Secretary;

(v) Director;

(vi) Senior Manager; and

(vii) Regional Manager.

(3) The Director, Loan Guaranty Service, Washington, DC, shall maintain a log listing all persons authorized to execute documents pursuant to paragraph (f) of this section and the dates such persons held such authority, together with certified copies of resolutions of the board of directors of the entity authorizing such individuals to perform the functions specified in paragraph (f)(1) of this section. These records shall be available for public inspection and copying at the Office of the Director of VA Loan Guaranty Service, Washington, DC 20420.

(Authority: 38 U.S.C. 3720(a)(5))

§ 36.4846 Cooperative loans.

(a) To be eligible for guaranty or insurance, any loan of the following types shall require prior approval of the Under Secretary for Benefits, 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 this subpart:

(1) Any loan which is related to an enterprise in which more than 10 individuals will participate; or

(2) Any loan 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.

(b) The issuance of such approval with respect to a 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; and

(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 than 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4847 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 Under Secretary for Benefits. 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 § 36.4847(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 § 36.4847(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 § 36.4847(d) 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 Under Secretary for Benefits. In the event of such an appeal, the Under Secretary for Benefits will review all relevant material concerning the matter and make a determination that shall constitute final agency action. If the lender's submission of 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 Under Secretary for Benefits will appoint a hearing officer or panel to conduct the hearing. When such additional proceedings are necessary, the Under Secretary for Benefits 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 Under Secretary for Benefits 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)

(The Office of Management and Budget has approved the information collections requirements of this section under control numbers 2900–0045 and 2900–0513.)

§ 36.4848 Servicer Appraisal Processing Program.

(a) *Delegation of authority to servicers to review liquidation appraisals and determine reasonable value.* Based on the reasonable value, the servicer will be able to determine net value.

(1) To be eligible for delegation of authority to review VA liquidation appraisals and determine the reasonable value for liquidation purposes on properties secured by VA guaranteed or insured 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 (SAR) acceptable to the Secretary.

(2) To qualify as a servicer's staff appraisal reviewer an applicant must be a full-time member of the servicer'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 Servicer Appraisal Processing Program (SAPP) staff appraisal reviewer. Three years of appraisal related experience is necessary to qualify as a servicer's staff appraisal reviewer. That experience must demonstrate 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. The individual must demonstrate the ability to review the work of others and to recognize deviations from accepted appraisal principle, practices, and techniques, error in computations, and unjustifiable and unsupportable conclusions.

(3) Servicers that have a staff appraisal reviewer determined

acceptable to VA, will be authorized to review liquidation appraisals and make reasonable value determinations for liquidation purposes on properties that are the security for VA guaranteed or insured loans. Additionally, servicers must satisfy initial 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 loan center in whose jurisdiction the servicer's staff appraisal reviewer is located before the SAPP authority may be utilized by that servicer in any other VA office's jurisdiction. To satisfy the initial office case review requirement, the first five cases of each servicer 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 servicer's notice of value. At that point, and prior to loan termination, each of the five cases will be submitted to the VA regional loan center having jurisdiction over the property. After a staff review of each case, VA will issue a notice of value which the servicer may use to compute the net value of the property for liquidation purposes. If these five cases are found to be acceptable by VA, the servicer's staff appraisal reviewer will be allowed to fully process subsequent appraisals for properties regardless of jurisdictional location without prior submission to VA and issuance by VA of a notice of value. Where the servicer's reviewer cannot readily meet the jurisdictional review requirement, the SAR applicant may request that VA expand the geographic area of consideration. VA will accommodate such requests if practicable. The initial office case review requirement may be expanded by VA if acceptable performance has not been demonstrated. After satisfaction of the initial office case review requirement, routine reviews of SAPP cases will be made by VA staff based upon quality control procedures established by the Undersecretary for Benefits. Such review will be made on a random sampling or performance related basis.

(4) Certifications required from the servicer will be specified with particularity in the separate instructions issued by the Secretary, as noted in § 36.4848(b).

(b) *Instructions for SAPP Procedures.* The Secretary will publish separate instructions for processing appraisals under the Servicer 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 SAPP cases. Due diligence is considered by VA to represent that care, as is to be properly expected from, and ordinarily exercised by, a reasonable and prudent servicer who would be dependent on the property as security to protect its investment.

(c) *Adjustment of value recommendations.* The amount of authority to upwardly adjust the fee appraiser's estimated market value during the servicer staff appraisal reviewer's initial review of the appraisal report or to subsequently process an appeal of the servicer's established reasonable value will be specified in the separate instructions issued by VA as noted in § 36.4848(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.

(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 appraiser's estimated market values or servicer's reasonable value determinations above the amount specified in the separate instructions issued by VA must be submitted, along with the servicer's recommendations, if any, to VA for processing and final determination. Unless otherwise authorized in the separate instructions servicers 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 servicer'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 servicer'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.

(d) *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 servicer under § 36.4848(c) 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.

(e) *Affiliations.* A servicer affiliated with a real estate firm, builder, land developer or escrow agent as a subsidiary division, or in any other entity in which it has a financial interest or which it owns may not use the authority for any cases involving the affiliate unless the servicer demonstrates to the Secretary's satisfaction that the servicer 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).

(f) *Quality control plans.* The servicer must have an effective self-policing or quality control system to ensure the adequacy and quality of their SAPP 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 servicer's independent internal audit division which reports directly to the firm's chief executive officer. The servicer 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 servicer's application of SAPP authority.

(g) *Fees.* The Secretary will require servicers to pay a $100.00 application fee for each SAR the servicer nominates for approval. The application fee will also apply if the SAR begins work for another servicer.

(h) *Withdrawal of servicer authority.* The authority for a servicer to determine reasonable value may be withdrawn by the Loan Guaranty Officer when proper cause exists. A servicer's authority to make reasonable value determinations shall be withdrawn when the servicer no longer meets the basic requirements for delegating the authority, or when it can be shown that the servicer'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 servicer or the servicer'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 SAPP 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 servicer'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 servicer 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 servicer'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 SAPP processing privileges. However, if within 15 days after receiving notice the servicer requests an opportunity to contest the withdrawal, the servicer 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 Loan Center Director who shall make the determination as to whether the action should be sustained, modified or rescinded. The servicer will be informed in writing of the decision.

(2) The servicer has the right to appeal the Regional Loan Center Director's decision to the Undersecretary for Benefits. In the event of such an appeal, the Undersecretary for Benefits will review all relevant material concerning the matter and make a determination that shall constitute final agency action. If the servicer's submission of opposition raises a genuine dispute over facts material to the withdrawal of SAPP authority, the servicer 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 Undersecretary for Benefits will appoint a hearing officer or panel to conduct the hearing. When such additional proceedings are necessary, the Undersecretary for Benefits shall base the determination on the facts as found, together with any information and argument submitted by the servicer.

(3) In actions based upon a conviction or civil judgment, or in which there is no genuine dispute over material facts, the Undersecretary for Benefits shall make a decision on the basis of all the information in the administrative record, including any submission made by the servicer.

(4) Withdrawal of the SAPP authority will require that VA make subsequent determinations of reasonable value for the servicer. Consequently, VA staff will review each appraisal report and issue a Notice of Value which can then be used by the servicer to compute the net value of properties for liquidation purposes.

(5) Withdrawal by VA of the servicer's SAPP authority does not prevent VA from also withdrawing automatic processing authority or taking debarment or suspension action based upon the same conduct of the servicer.

(Authority 38 U.S.C. 3703(c)(1), 3731 and 3732)

(The Office of Management and Budget has approved the information collection requirements in this section under control numbers 2900–0045 and 2900–0513.)

§ 36.4849 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.

(Authority 38 U.S.C. 3703(c)(1))

§ 36.4850 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 (l) 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.* Before February 1st 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 stages of delinquency. However, at a minimum the holder's collection procedures must include the following actions:

(i) An effort, concurrent with the initial late payment 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.

(ii) 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.

(iii) 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.

(iv)(A) A letter to the borrower if payment has not been received:

(*1*) In the case of a default occurring within the first 6 months following loan closing or the execution of a modification agreement pursuant to § 36.4815, within 45 calendar days after such payment was due; or

(*2*) In the case of any other default, within 75 calendar days after such payment was due.

(B) The letter required by paragraph (g)(1)(iv)(A) must be mailed no later than 7 calendar days after the payment is delinquent for the time period stated in paragraph (g)(1)(iv)(A) and shall:

(*1*) Provide the borrower with a toll-free telephone number and, if available, an e-mail address for contacting the servicer;

(*2*) Explain loss mitigation options available to the borrower;

(*3*) Emphasize that the intent of servicing is to retain home ownership whenever possible; and

(*4*) Contain the following language:

The delinquency of your mortgage loan is a serious matter that could result in the loss of your home. If you are the veteran whose entitlement was used to obtain this loan, you can also lose your entitlement to a future VA home loan guaranty. If you are not already working with us to resolve the delinquency, please call us to discuss your workout options. You may be able to make special payment arrangements that will reinstate your loan. You may also qualify for a repayment plan or loan modification.

VA has guaranteed a portion of your loan and wants to ensure that you receive every reasonable opportunity to bring your loan current and retain your home. VA can also answer any questions you have regarding your entitlement. If you have access to the Internet and would like to obtain more information, you may access the VA web site at *www.va.gov.* You may also learn where to speak to a VA Loan Administration representative by calling 1–800–827–1000.

(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 2 CFR parts 180 and 801.

(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 60 calendar days delinquent, if the property is abandoned, this fact must be reported to the Secretary as required in § 36.4817(c)(10) and immediate action should be initiated by the servicer to terminate the loan once the abandonment has been confirmed.

(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) *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.

(l) *Provision of Data.* Holders shall provide available statistical data on delinquency and foreclosure rates and their analysis of such data to the Secretary upon request.

(Authority 38 U.S.C. 3703(c)(1))

(The Office of Management and Budget has approved the information collection requirements in this section under Control Number 2900–0530.)

§ 36.4851 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).

(Authority 38 U.S.C. 3703(c)(1))

§ 36.4852 Authority to close loans on the automatic basis.

(a) *Supervised lender authority.* Supervised lenders of the classes described in 38 U.S.C. 3702(d)(1) and (2) are authorized by statute 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) *Non-supervised lender authority.* Non-supervised 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. Each of the minimum requirements listed below must be met by applicant lenders.

(1) *Experience.* The applicant lender must meet one of the following experience requirements:

(i) The applicant lender must have been actively engaged in originating VA loans for at least two years, have a VA Lender ID number and have originated and closed a minimum of ten VA loans within the past two years, excluding interest rate reduction refinance loans (IRRRLs), that have been properly documented and submitted in compliance with VA requirements and procedures; or

(ii) The applicant lender must have a VA ID number and, if active for less than two years, have originated and closed at least 25 VA loans, excluding IRRRLs, that have been properly documented and submitted in compliance with VA requirements and procedures; or

(iii) Each principal officer of the applicant lender, who is actively involved in managing origination functions, must have a minimum of two recent years' management experience in the origination of VA loans. This experience may be with the current or prior employer. For the purposes of this requirement, principal officer is defined as president or vice president; or

(iv) If the applicant lender has been operating as an agent for a non-supervised automatic lender (sponsoring lender), the firm must submit documentation confirming that it has a VA Lender ID number and has originated a minimum of ten VA loans, excluding IRRRLs, over the past two years. If active for less than two years, the agent must have originated at least 25 VA loans. The required documentation is a copy of the VA letter approving the applicant lender as an agent for the sponsoring lender; a copy of the corporate resolution, describing the functions the agent was to perform, submitted to VA by the sponsoring lender; and a letter from a senior officer of the sponsoring lender indicating the number of VA loans submitted by the agent each year and that the loans have been properly documented and submitted in compliance with VA requirements and procedures.

(2) *Underwriter.* A senior officer of the applicant lender must nominate a full-time qualified employee(s) to act in the applicant lender's behalf as underwriter(s) to personally review and make underwriting decisions on VA loans to be closed on the automatic basis.

(i) Nominees for underwriter must have a minimum of three years experience in processing, pre-underwriting or underwriting mortgage loans. At least one recent year of this experience must have included making underwriting decisions on VA loans. (Recent is defined as within the past three years.) A VA nomination and current resume, outlining the underwriter's specific experience with

VA loans, must be submitted for each underwriter nominee.

(ii) Alternatively, if an underwriter does not have the experience outlined above, the underwriter must submit documentation verifying that he or she is a current Accredited Residential Underwriter (ARU) as designated by the Mortgage Bankers Association (MBA).

(iii) If an underwriter is not located in the lender's corporate office, then a senior officer must certify that the underwriter reports to and is supervised by an individual who is not a branch manager or other person with production responsibilities.

(iv) All VA-approved underwriters must attend a 1-day (eight-hour) training course on underwriter responsibilities, VA underwriting requirements, and VA administrative requirements, including the usage of VA forms, within 90 days of approval (if VA is unable to make such training available within 90 days, the underwriter must attend the first available training). Immediately upon approval of a VA underwriter, the office of jurisdiction will contact the underwriter to schedule this training at a VA regional office (VARO) of the underwriter's choice. This training is required for all newly approved VA underwriters, including those who qualified for approval based on an ARU designation, as well as VA-approved underwriters who have not underwritten VA-guaranteed loans in the past 24 months. Furthermore, and at the discretion of any VARO in whose jurisdiction the lender is originating VA loans, VA-approved underwriters who consistently approve loans that do not meet VA credit standards may be required to retake this training.

(3) *Underwriter Certification.* The lender must certify that all underwriting decisions as to whether to accept or reject a VA loan will be made by a VA-approved underwriter. In addition each VA-approved underwriter will be required to certify on each VA loan that he or she approves that the loan has been personally reviewed and approved by the underwriter.

(4) *Financial Requirements.* Each application must include the most recent annual financial statement audited and certified by a certified public accountant (CPA). If the date of the annual financial statement precedes that of the application by more than six months, the lender must also attach a copy of its latest internal financial statement. Lenders are required to meet either the working capital or the minimum net worth financial requirement as defined below.

(i) *Working Capital.* A minimum of $50,000 in working capital must be demonstrated.

(A) Working capital is a measure of an applicant lender's liquidity, or the ability to pay its short-term debts. Working capital is defined as the excess of current assets over current liabilities. Current assets are defined as cash or other liquid assets convertible into cash within a 1-year period. Current liabilities are defined as debts that must be paid within the same 1-year time frame.

(B) The VA determination of whether a lender has the required minimum working capital is based on the balance sheet of the lender's annual audited financial statement. Therefore, either the balance sheet must be classified to distinguish between current and fixed assets and between current and long-term liabilities or the information must be provided in a footnote to the statement.

(ii) *Net Worth.* Lenders must show evidence of a minimum of $ 250,000 in adjusted net worth. Net worth is a measure of an applicant lender's solvency, or its ability to exist in the long run, quantified by the payment of long-term debts. Net worth as defined by generally accepted accounting principles (GAAP) is total assets minus total liabilities. Adjusted net worth for VA purposes is the same as the adjusted net worth required by the Department of Housing and Urban Development (HUD), net worth less certain unacceptable assets including:

(A) Any assets of the lender pledged to secure obligations of another person or entity.

(B) Any asset due from either officers or stockholders of the lender or related entities, in which the lender's officers or stockholders have a personal interest, unrelated to their position as an officer or stockholder.

(C) Any investment in related entities in which the lender's officers or stockholders have a personal interest unrelated to their position as an officer or stockholder.

(D) That portion of an investment in joint ventures, subsidiaries, affiliates and/or other related entities which is carried at a value greater than equity, as adjusted. ''Equity as adjusted'' means the book value of the related entity reduced by the amount of unacceptable assets carried by the related entity.

(E) All intangibles, such as goodwill, covenants not to compete, franchisee fees, organization costs, etc., except unamortized servicing costs carried at a value established by an arm's-length transaction and presented in accordance with generally accepted accounting principles.

(F) That portion of an asset not readily marketable and for which appraised values are very subjective, carried at a value in excess of a substantially discounted appraised value. Assets such as antiques, art work and gemstones are subject to this provision and should be carried at the lower of cost or market.

(G) Any asset that is principally used for the personal enjoyment of an officer or stockholder and not for normal business purposes. Adjusted net worth must be calculated by a CPA using an audited and certified balance sheet from the lender's latest financial statements. ''Personal interest'' as used in this section indicates a relationship between the lender and a person or entity in which that specified person (e.g., spouse, parent, grandparent, child, brother, sister, aunt, uncle or in-law) has a financial interest in or is employed in a management position by the lender.

(5) *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 submitted to VA and the applicant must agree that VA may contact the named source(s) for the purpose of verifying the information. A line of credit must be unrestricted, that is, funds are available upon demand to close loans and are not dependent on prior investor approval. A letter from the company(ies) verifying the unrestricted line(s) of credit must be submitted with the application for automatic authority.

(6) *Permanent investors.* If the lender customarily sells loans it originates, it must have a minimum of two permanent investors. The names, addresses and telephone numbers of the permanent investors must be submitted with the application.

(7) *Liaison.* The lender applicant must designate an employee and an alternate to be the primary liaison with VA. The liaison officers should be thoroughly familiar with the lender's entire operation and be able to respond to any query from VA concerning a particular VA loan or the firm's automatic authority.

(8) *Other considerations.* All applications will also be reviewed in light of the following considerations:

(i) There must be no factors that indicate that the firm would not exercise the care and diligence required of a lender originating and closing VA loans on the automatic basis; and

(ii) In the event the applicant lender, any member of the board of directors, or any principal officer has ever been debarred or suspended by any Federal agency or department, or any of its directors or officers has 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 be submitted with the application for automatic authority.

(9) *Quality Control System.* In order to be approved as a non-supervised 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 lender 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.

(10) *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.

(11) *Probation.* Lenders meeting these requirements will be approved to close VA loans on an automatic basis for a 1-year period. At the end of this period, the lender's quality of underwriting, the completeness of loan submissions, compliance with VA requirements and procedures, and the delinquency and foreclosure rates will be reviewed.

(12) *Extensions of Automatic Authority.* When a lender wants its automatic authority extended to another State, the request must be submitted, with the fee designated in paragraph (e)(5) of this section, to the VA regional office having jurisdiction in the State where the lender's corporate office is located.

(i) When a lender wants its automatic authority to include loans involving a real estate brokerage and/or a residential builder or developer in which it has a financial interest, owns, is owned by, or with which it is affiliated, the following documentation must be submitted:

(A) A corporate resolution from the lender and each affiliate indicating that they are separate entities operating independently of each other. The lender's corporate resolution must indicate that it will not give more favorable underwriting consideration to its affiliate's loans, and the affiliate's corporate resolution must indicate that it will not seek to influence the lender to give their loans more favorable underwriting consideration.

(B) Letters from permanent investors indicating the percentage of all VA loans based on the affiliate's production originated by the lender over a 1-year period that are past due 90 days or more. This delinquency ratio must be no higher than the national average for the same period for all mortgage loans.

(ii) When a lender wants its automatic authority extended to additional States, the lender must indicate how it plans to originate VA loans in those States. Unless a lender proposes a telemarketing plan, VA requires that a lender have a presence in the State, that is, a branch office, an agent relationship, or that it is a reasonable distance from one of its offices in an adjacent State, i.e., 50 miles. If the request is based on an agency relationship, the documentation outlined in paragraph (b)(13) must be submitted with the request for extension.

(13) *Use of Agents.* A lender using an agent 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 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. Lenders requesting an agent must submit the following documentation to the VA regional office having jurisdiction for the lender's corporate office:

(i) A corporate resolution certifying that the lender takes full responsibility for all acts, errors and omissions of the agent that it is requesting. The corporate resolution must also identify the agent's name and address, and the geographic area in which the agent will be originating and/or closing VA loans; whether the agent is authorized to issue interest rate lock-in agreements on behalf of the lender; and outline the functions the agent is to perform. Alternatively, the lender may submit a blanket corporate resolution which sets forth the functions of any and all agents and identifies individual agents by name, address, and geographic area in separate letters which refer to the blanket resolution.

(ii) When the VA regional office having jurisdiction for the lender's corporate office acknowledges receipt of the lender's request in writing, the agent is thereby authorized to originate VA loans on the lender's behalf.

(Authority: 38 U.S.C. 501(a), 3702(d))

(c) *Reporting responsibility.* A lender approved to close loans on the automatic basis who subsequently fails to meet the requirements of this section must report to VA the circumstances surrounding the deficiency and the remedial action to be taken to cure it. Failure to advise VA in a timely manner could result in a lender's loss of its approval to close VA loans on the automatic basis.

(Authority: 38 U.S.C. 501(a), 3702(d))

(d) *Annual recertification.* Non-supervised lenders of the class described in 38 U.S.C. 3702(d)(3) must be recertified annually for authority to process loans on the automatic basis. The following minimum annual recertification requirements must be met by each lender approved for automatic authority:

(1) *Financial requirements.* A lender must submit, within 120 days following the end of its fiscal year, an audited and certified financial statement with a classified balance sheet or a separate

footnote for adjusted net worth to VA Central Office (264) for review. The same minimum financial requirements described in § 36.4852(b)(5) must be maintained and verified annually in order to be recertified for automatic authority.

(2) *Processing annual lender data.* The VA regional office having jurisdiction for the lender's corporate office will mail an annual notice to the lender requesting current information on the lender's personnel and operation. The lender is required to complete the form and return it with the appropriate annual renewal fees to the VA regional office.

(Authority: 38 U.S.C. 501(a), 3702(d))

(e) *Lender fees.* To participate as a VA automatic lender, non-supervised lenders of the class described in 38 U.S.C. 3702(d)(3) 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) A minimum fee of $100 for any other VA administrative action pertaining to a lender's status as an automatic lender;

(6) $200 annually for certification of home offices; and

(7) $100 annually for each agent renewal.

(f) *Supervised lender fees.* 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 fee for each agent approval; and

(2) $100 annually for each agent renewal.

(Authority: 38 U.S.C. 501(a) and 3703(c)(1))

(g) *LAPP fees.* Lenders participating in VA's Lender Appraisal Processing Program shall pay a fee of $100 for approval of each staff appraisal reviewer.

(Authority 38 U.S.C. 3703(c)(1))

§ 36.4853 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 authority of both supervised and non-supervised 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 at any time for failure to meet basic qualifying and/or annual recertification criteria.

(i) *Non-supervised lenders.* (A) Automatic authority may be withdrawn for lack of a VA-approved underwriter, failure to maintain $50,000 in working capital or $250,000 in adjusted net worth, or failure to file required financial information.

(B) During the 1-year probationary period for newly approved lenders, automatic authority may be temporarily or permanently withdrawn for any of the reasons set forth in this section regardless of whether deficiencies previously have been brought to the attention of the probationary lender.

(ii) *Supervised lenders.* Automatic authority will be withdrawn for 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).

(Authority: 38 U.S.C. 3702(d))

(3) Automatic processing authority may also be withdrawn for any of the causes for debarment set forth in 2 CFR parts 180 and 801.

(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 may occur when:

(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 may occur when:

(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 veteran 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 may occur when:

(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 non-supervised 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 Under Secretary for Benefits 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 Under Secretary for Benefits 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 Under Secretary for Benefits 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. 3703(c)(1))

(The Office of Management and Budget has approved the information collection requirements in this section under control numbers 2900–0574.)

§ 36.4854 Estate of veteran in real property.

(a) The title of 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 and on which construction, or repairs, or alterations or improvements are to be made, 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. Such estate 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 Under Secretary for Benefits, 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; or

(4) A beneficial interest in a revocable Family Living Trust that ensures that the veteran, or veteran and spouse, have an equitable life estate, provided the lien attaches to any remainder interest and the trust arrangement is valid under State law.

(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; or

(5) Sale and lease restrictions:

(i) Except as to condominiums, the right in any grantor or cotenant in the chain of 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 § 36.4862(c).

(iv) Notwithstanding the provisions of paragraphs (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.

(*4*) 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.

(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, 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) 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 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 than 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. 3703(c))

§ 36.4855 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 § 36.4854(a).

(Authority 38 U.S.C. 3703(c)(1))

§ 36.4856 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, Under Secretary for Benefits, 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.

(Authority: 38 U.S.C. 3703(d)(3))

§ 36.4857 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4858 [Reserved]

§ 36.4859 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.

(b) 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.

(c) Such loans shall be secured as required in § 36.4855: *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*, that 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.

(d) 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.

(Authority: 38 U.S.C. 3703(c)(1), 3710(b)(6))

§ 36.4860 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 36.4857, 36.4859, and 36.4869 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 this subpart, 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 § 36.4801, Condominium).

(3) *Conversion condominium.* Condominium projects not originally built and sold as condominiums but

subsequently converted to the 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 owner's 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 or 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. An 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 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. 3703(c)(1), (d)(3), 3710(a)(6))

§ 36.4861 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. 3710(a)(6))

(b) *Estate of unit owner.* The legal estate of each unit owner must comply with the provisions of § 36.4854. 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 that condominium.

(Authority: 38 U.S.C. 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 owner's 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 (§§ 36.4864(a)(3) and 36.4865(b)(6)).

(Authority: 38 U.S.C. 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 § 36.4864(a)(6).)

(Authority: 38 U.S.C. 3703(c)(1), 3710(a)(6))

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0448.)

§ 36.4862 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.

(iii) 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. 3704(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 a 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 § 36.4856. 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. 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 that 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) *Encroachments*—(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 or 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 shown 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 § 36.4854(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 § 36.4854(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 § 36.4809(e) or § 36.4854(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. 3703(c)(1), 3710(a)(6))

§ 36.4863 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,

(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, or

(iii) On a case basis, modifications or variations of the requirements of paragraphs (a)(1)(i) and (ii) of this section 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 the declarant owns.

(3) *Unit owners' participation in management.* Declarant 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 § 36.4829. 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. 3703(c)(1), 3710(a)(6))

§ 36.4864 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 (§ 36.4861(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 § 36.4865(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 project 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 §§ 36.4861(b) and 36.4862(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 basic, 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 § 36.4800 series.

(Authority: 38 U.S.C. 3703(c)(1), 3710(a)(6))

(The Office of Management and Budget has approved the information collection requirements of this section under control number 2900–0448.)

§ 36.4865 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 MPRs (Minimum Property Requirements) and are safe, sanitary, and structurally sound. The Department of Veterans Affairs MPRs 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. 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 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. 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 equipment.

(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. 3703(c)(1), 3710(a)(6))

(5) *Information brochure/public offering statement*. When units are being sold by the declarant (not applicable to resales), an information brochure/public offering statement must be given to veteran buyers prior to the time a down payment is received and an agreement is signed, unless State law authorized receipt of the down payment 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 § 36.4865(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 any condominium project 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. If 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 association of owners 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 for consent of the association and the 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. 3703(c)(2), 3710(a)(6))

(The Office of Management and Budget has approved the information collection requirements in this section under control number 2900–0448.)

§ 36.4867 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 §§ 36.4860 through 36.4865, 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.

(Authority: 38 U.S.C. 3703(c)(1), 3705)

§ 36.4868 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.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4869 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 not later than 4 years after 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 a 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 Under Secretary for Benefits.

(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.

(Authority: 38 U.S.C. 3703(c)(1), 3727)

§ 36.4870 Advertising and solicitation requirements.

Any advertisement or solicitation in any form (*e.g.*, written, electronic, oral) from a private lender concerning housing loans to be guaranteed or insured by the Secretary:

(a) Must not include information falsely stating or implying that it was issued by or at the direction of VA or any other department or agency of the United States, and

(b) Must not include information falsely stating or implying that the lender has an exclusive right to make loans guaranteed or insured by VA.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4875 Insured loan and insurance account.

(a) Loans otherwise eligible may be insured when purchased by a lender eligible under 38 U.S.C. 3703(a) if the purchaser (lender) submits with the loan report evidence of an agreement, general or special, made prior to the closing of the loan, to purchase such loan subject to its being insured.

(b) A current account shall be maintained in the name of each insured lender or purchaser. The account shall be credited with the appropriate amounts available for the payment of losses on insured loans made or purchased. The account shall be debited with appropriate amounts on account of transfers, purchases under § 36.4820, or payment of losses. The Secretary may on 6 months' notice close any lender's insurance account. Such account after expiration of the 6-month period shall be available only as to loans embraced therein.

(c) Amounts received or recovered by the Secretary or the holder with respect to a loan after payment of an insured claim thereon will not restore any amount to the holder's insurance account.

(Authority: 38 U.S.C. 3703(a)(2))

§ 36.4877 Transfer of insured loans.

(a) In cases involving the transfer from one insured financial institution to another insured institution of loans which are transferred without recourse, guaranty, or repurchase agreement, if no payment on any loan included in the transfer is past due more than one calendar month at the time of transfer there shall be transferred from the insurance account of the transferor to the insurance account of the transferee an amount equal to the original percentage credited to the insurance account in respect to each loan being transferred applied to the unpaid balance of such loans, or to the purchase price, whichever is the lesser.

(b) Transfers between insurance accounts in a manner or under conditions not provided in paragraph (a) of this section must have the prior approval of the Secretary.

(c) Where loans are transferred with recourse or under a guaranty or repurchase agreement no insurance credit will be transferred or insurance account affected and no reports will be required.

(d) In all cases of transfer of loans from one insured financial institution to another insured institution, except as provided in paragraph (c) of this section, a report on a prescribed form executed by the parties and showing their agreement with regard to the transfer of insurance credits shall be made to the Secretary.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4878 Debits and credits to insurance account under § 36.4820.

In the event that an insured loan is transferred under the provisions of § 36.4820, there shall be charged to the insurance account of the transferor a sum equal to the amount paid transferor on account of the indebtedness less the current market value of the property transferred as security therefor as determined by an appraiser designated by the Secretary, or the amount chargeable to such insurance account in the event of a transfer under § 36.4877, whichever sum is the greater. The credit to the insurance account of the transferee will be computed in accordance with § 36.4877(a).

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4879 Payment of insurance.

(a) Upon the continuance of a default for a period of three months, the holder may proceed to establish the net loss, after giving the notices prescribed in §§ 36.4817 and 36.4850 if security is available. The net loss shall be reported to the Secretary with proper claim, whereupon the holder shall be entitled to payment of the claim within the amount then available for such payment under the payee's related insurance account. Subject to the provisions of the paragraph (b) of this section and to § 36.4875(b) a supplemental claim for any balance of an insurance loss may be filed at any time within 5 years after the date of the original claim.

(b) The basis of the claim for an insured loss shall consist in the unrealized principal or the amount paid for the obligation, if less, plus unrealized interest to the date of claim or the date of sale whichever is earlier, and those expenses, if any, allowable under § 36.4814, but subject to proper credits because of payments, set-off, proceeds of security or otherwise, provided that if there is no liquidation of security the claim shall not include an accrual of interest for a period in excess of 6 months from the date of the first uncured default.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4880 Reports of insured institutions.

An insured financial institution shall make such reports respecting its insurance accounts as the Secretary may from time to time require, not more frequently than semiannually.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4890 Purpose.

Sections 36.4890 through 36.4893 are promulgated to achieve the aims of the applicable provisions of Executive Orders 11246 and 11375 and the regulations of the Secretary of Labor with respect to federally assisted construction contracts.

§ 36.4891 Applicability.

(a) For the purposes of the home loan guaranty and insurance and direct loan programs of the Department of Veterans Affairs, the term ''applicant for Federal assistance'' or ''applicant'' in Part III of Executive Order 11246, shall mean the builder, sponsor or developer of land to be improved by such builder, sponsor or developer for the purpose of constructing housing thereon for sale to eligible veterans with financing which is to be guaranteed or insured or made under the provisions of 38 U.S.C. chapter 37, or the builder, sponsor or developer of housing to be constructed for sale to eligible veterans with financing which is to be guaranteed or insured or made under the provisions of 38 U.S.C. chapter 37.

(b) The provisions of Executive Orders 11246 and 11375 and the rules and regulations of the Secretary of Labor are applicable to:

(1) Each Master Certificate of Reasonable Value or extension or modification thereof relating to proposed construction issued on or after July 22, 1963;

(2) Each individual Certificate of Reasonable Value or extension or modification thereof relating to proposed construction issued on or after July 22, 1963, except as provided in paragraph (c)(2) of this section;

(3) Each Special Conditions Letter or modification thereof issued on or after July 22, 1963, in respect to site approval of land to be improved by a builder, sponsor or developer for the construction of housing thereon; and

(4) Each direct loan fund reservation commitment or extension thereof issued to builders on or after July 22, 1963.

(c) The provisions of Executive Orders 11246 and 11375 and the rules and regulations of the Secretary of Labor are not applicable to:

(1) Grants under chapter 21, title 38, U.S.C.;

(2) Individual Certificates of Reasonable Value issued on or after July 22, 1963, if:

(i) The certificate relates to existing properties, either previously occupied or unoccupied; or

(ii) The certificate relates to proposed construction and—

(A) A veteran was named in the request for appraisal, or

(B) A veteran contracted for the construction or purchase of the home prior to issuance of the certificate, or

(C) The property was listed in the Schedule of Reasonable Values on an outstanding Master Certificate of Reasonable Value issued prior to July 22, 1963;

(3) Any contract or subcontract for construction work not exceeding $10,000; and

(4) Any other contract or subcontract which is exempted or excepted by the regulations of the Secretary of Labor.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4892 Certification requirements.

In any case in which §§ 36.4890 through 36.4893 are applicable, as set forth in § 36.4891, no action will be taken by the Department of Veterans Affairs on any request for appraisal relating to proposed construction, site approval of land to be improved by a builder, sponsor or developer for the construction of housing thereon, or for a direct loan fund reservation commitment unless the builder, sponsor or developer has furnished the Department of Veterans Affairs a signed certification in form as follows:

To induce the Department of Veterans Affairs to act on any request submitted by or on behalf of the undersigned for site approval of land to be improved for the construction of housing thereon to be financed with loans guaranteed, insured or made by the Department of Veterans Affairs, or for establishment by the Department of Veterans Affairs of reasonable value relating to proposed construction or for direct loan fund reservation commitments, the undersigned hereby agrees that it will incorporate or cause to be incorporated into any contract for construction work or modification thereof, as defined in the rules and regulations of the Secretary of Labor relating to the land or housing included in its request to the Department of Veterans Affairs the following equal opportunity clause:

During the performance of this contract the contractor agrees as follows:

(1) The contractor will not discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin. The contractor will take affirmative action to ensure that applicants are employed, and that employees are treated during employment without regard to their race, color, religion, sex or national origin. Such action shall include, but not be limited to the following: Employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The contractor agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided setting forth the provisions of this nondiscrimination clause.

(2) The contractor will, in all solicitations or advertisements for employees placed by or on behalf of the contractor, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex or national origin.

(3) The contractor will send to each labor union or representative of workers with which he has a collective bargaining agreement or other contract or understanding, a notice to be provided advising the said labor union or workers' representative of the contractor's commitments under section 202 of Executive Order 11246 of September 24, 1965, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(4) The contractor will comply with all provisions of Executive Order 11246 of September 24, 1965, and of the rules, regulations and relevant orders of the Secretary of Labor.

(5) The contractor will furnish all information and reports required by Executive Order 11246 of September 24, 1965, and by the rules, regulations and orders of the Secretary of Labor, or pursuant thereto, and will permit access to his books, records and accounts by the administering agency and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations and orders.

(6) In the event of the contractor's noncompliance with the nondiscrimination clauses of this contract or with any of the said rules, regulations or orders, this contract may be canceled, terminated or suspended in whole or in part and the contractor may be declared ineligible for further Government contracts or federally assisted construction contracts in accordance with procedures authorized in Executive Order 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in Executive Order 11246 of September 24, 1965, or by rule, regulation or order of the Secretary of Labor, or as otherwise provided by law.

(7) The contractor will include the provisions of paragraphs (1) through (7) in every subcontract or purchase order unless exempted by rules, regulations or orders of the Secretary of Labor issued pursuant to section 204 of Executive Order 11246 of September 24, 1965, so that such provisions will be binding upon each subcontractor or vendor. The contractor will take such action with respect to any subcontract or purchase order as the administering agency may direct as a means of enforcing such provisions, including sanctions for noncompliance: Provided, however, That in the event a contractor becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by the agency, the contractor may request the United States to enter into such litigation to protect the interests of the United States.

Except in special cases and in subcontracts for the performance of construction work at the site of construction, the clause is not required to be inserted in subcontracts below the second tier. Subcontracts may incorporate by reference the equal opportunity clause.

The undersigned further agrees that it will be bound by the above equal opportunity clause in any federally assisted construction work which it performs itself other than through the permanent work force directly employed by an agency of Government.

The undersigned agrees that it will cooperate actively with the administering agency and the Secretary of Labor in obtaining the compliance of contractors and subcontractors with the equal opportunity clause and the rules, regulations and relevant orders of the Secretary of Labor, that it will furnish the administering agency and the Secretary of Labor such information as they may require for the supervision of such compliance, and that it will otherwise assist the administering agency in the discharge of the agency's primary responsibility for securing compliance. The undersigned further agrees that it will refrain from entering into any contract or contract modification subject to Executive Order 11246 with a contractor debarred from, or who has not demonstrated eligibility for, Government contracts and federally assisted construction contracts pursuant to Part II, Subpart D of Executive Order 11246 and will carry out such sanctions and penalties for violation of the equal opportunity clause as may be imposed upon the contractors and subcontractors by the administering agency or the Secretary of Labor pursuant to Part II, Subpart D of Executive Order 11246.

In addition, the undersigned agrees that if it fails or refuses to comply with these undertakings such failure or refusal shall be a proper basis for cancellation by the Department of Veterans Affairs of any outstanding master certificates of reasonable value or individual certificates of reasonable value relating to proposed construction, except in respect to cases in which an eligible veteran has contracted to purchase a property included on such certificates, and for the rejection of future requests submitted by the undersigned or on his or her behalf for site approval, appraisal services, and direct loan fund reservation commitments until satisfactory assurance of future compliance has been received from the undersigned, and for referral of the case to the Department of Justice for appropriate legal proceedings.

(Authority: 38 U.S.C. 3703(c)(1))

§ 36.4893 Complaint and hearing procedure.

(a) Upon receipt of a written complaint signed by the complainant to the effect that any person, firm or entity has violated the undertakings referred to in § 36.4892, such person, firm or other entity shall be invited to discuss the matter in an informal hearing with the Director of the Department of Veterans Affairs regional office or center.

(b) If the existence of a violation is denied by the person, firm or other entity against which a complaint has been made, the Director or designee shall conduct such inquiries and hearings as may be deemed appropriate for the purpose of ascertaining the facts.

(c) If it is found that the person, firm or other entity against which a complaint has been made has not violated the undertakings referred to in § 36.4892, the parties shall be so notified.

(d) If it is found that there has been a violation of the undertakings referred to in § 36.4892, the person, firm or other entity in violation shall be requested to attend a conference for the purpose of discussing the matter. Failure or refusal to attend such a conference shall be proper basis for the application of sanctions.

(e) The conference arranged for discussing a violation shall be conducted in an informal manner and shall have as its primary objective the elimination of the violation. If the violation is eliminated and satisfactory assurances are received that the person, firm or other entity in violation will comply with the undertakings pursuant to § 36.4892 in the future, the parties concerned shall be so notified.

(f) Failure or refusal to comply and give satisfactory assurances of future compliance with the equal employment opportunity requirements shall be proper basis for applying sanctions. The sanctions shall be applied in accordance with the provisions of Executive Order 11246 as amended and the regulations of the Secretary of Labor.

(g) Upon written application, a complainant or a person, firm or other entity against which a complaint has been filed may apply to the Under Secretary for Benefits for a review of the action taken by a Director. Upon receiving such application, the Under Secretary for Benefits may designate a representative or representatives to conduct an informal hearing and to make a report of findings. The Under Secretary for Benefits may, after a review of such report, modify or reverse an action taken by a Director.

(h) Reinstatement of restricted persons, firms or other entities shall be within the discretion of the Under Secretary for Benefits and under such terms as the Under Secretary for Benefits may prescribe.

(Authority 38 U.S.C. 3703(c)(1))

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