CHAPTER 11. MORTGAGE CREDIT REQUIREMENTS FOR SALES TYPE COOPERATIVES

11-1. GENERAL. Mortgage Credit analysis of sales type cooperative projects proceeds logically in the steps listed below. In order to orient these steps with the over-all progress of the project, certain steps are listed in parentheses that are not a part of Mortgage Credit Analysis.

a. Determination of Amount and Amortization Period of Loan.

b. Determination of Estimated Requirements for Completion of Project (Issuance of Commitment).

c. Credit Investigation.

d. Analysis of Acceptability of Member Cooperators.

e. Determination of Acceptability of Cooperative Organization.

f. Assurance of Completion (Initial Endorsement of Mortgage).

g. Insurance of Advances.

h. Construction Changes (Final-Endorsement of Mortgage).

i. Insurance of Individual Mortgages.

j. Substitution of Mortgagors.

11-2. AMOUNT OF LOAN. The initial step in Mortgage Credit processing subsequent to receipt of an application involves the determination of the amount and amortization period of loan. The amount of mortgage loan will be the amount applied for but not to exceed the maximum amount permitted under the statutory and regulatory limitations under Section 213 of the National Housing Act.

a. The Mortgage must involve a principal obligation in an even multiple of $100 and a term not to exceed 35 years.

b. Amount of Loan - New Construction - (Existing units to be rehabilitated or reconstructed are not eligible.) Insurable mortgage amount shall not exceed the lowest of:

(1) $12,500,000 to a private mortgagor as defined in the FHA Regulations under Section 213.1(c).

(2) The sum of the unit mortgage amounts for each single family unit comprising the project. Unit mortgage amounts in the above computation would be limited to the maximum mortgage available to a single family owner occupant under Section 203(b)(2).

NOTE: Leaseholds are not acceptable under Sales Type Cooperatives except with prior approval of the Assistant Secretary-FHA Commissioner.

(3) The sum of the unit mortgage amounts, computed on the basis of a separate mortgage for each single-family dwelling comprising the project which would meet the minimum cash investment requirements for Section 203(b), based on the total cost of acquisition. (See Reference (6) of the Foreword.)

(4) For the purpose of determining the unit mortgage amounts under this limitation any required deposits for working capital and items of prepaid expense shall not be included in the total cost of acquisition.

(5) This limitation is applied prior to closing.

11-3. AMORTIZATION PERIOD OF LOAN. The mortgage must be amortized during a period not in excess of 3/4 of the remaining economic life of the physical improvements or 35 years from the beginning of amortization, whichever is the lesser. Amortization shall be in accordance with the Basic Multifamily Amortization Plans, Section 213, Cooperative Housing, FHA Form 3010.

11-4. THE DETERMINATION OF THE MAXIMUM INSURABLE MORTGAGE is accomplished by completing Part I of FHA Form 2264-A. Part II of this form details the total requirements for Project Settlement. Funds required for cash investment, initial operating deficit, commitment fees, marketing fees, discount(s) and off site construction costs are set forth. Part III reflects the source of funds to meet project cash requirements. FHA Form 2264-A is completed in accordance with instructions in Reference (3) of the Foreword.

After determination of the maximum insurable mortgage and estimated requirements for completion of the project, it is necessary to determine the unit replacement cost and the unit mortgage amount (original release price) for each unit in the project. This information is entered on FHA Form 2461. Instructions for the calculation of these items and completion of the form are contained in Reference (3) of the Foreword.

11-5. ELIGIBLE FOR INSURANCE. If the case appears eligible for insurance (subject to approval of the mortgagor and the members) the Multifamily Coordinator/ADTS prepares a report on FHA Form 2438 indicating the terms of a commitment which are justified by the findings contained in the various Underwriting reports.

11-6. PRESALE REQUIREMENT. In cases involving the insurance of advances of mortgage proceeds, the recommendation for the issuance of the commitment must be conditioned upon approval of the proposed mortgagor and 100% of its members prior to closing and initial endorsement of the credit instrument. In cases involving insurance upon completion the recommendation must be conditioned upon the approval of 100% of the members prior to initial-final endorsement of the credit instrument.

11-7. CREDIT INVESTIGATION. Subsequent to issuance of commitment and prior to the setting of a date for closing, the mortgagee must submit a statement of the cost to the mortgagor and the Cooperative Membership Exhibit, FHA Form 3203, in duplicate. The number of members must equal the total number of family units in the project.

a. The Cooperative membership Exhibit includes a statement showing the name of each proposed member of the cooperative, the type of dwelling unit he will occupy, total acquisition cost (exclusive of any required working capital deposit), total amount of down payment required, and amount of monthly charge to each member to cover debt service, operating expense, taxes and special assessments, if any. This statement must be signed by a responsible officer of the cooperative. To this exhibit must be attached a credit report on each individual listed therein, his signed personal financial statement, and verification of employment and bank accounts. The personal financial statements should be prepared on FHA Form 2900-1 with copy 2900-2 attached.

(11-7) b. Cooperative Membership Exhibit Information. The Cooperative Membership Exhibit and attachments provide information regarding the credit standing and paying ability of the members. If the exhibit is incomplete, additional information or verification should be requested. Both copies of this exhibit, together with any other credit data which are collected, should be placed in the Credit Binder for the proposed Section 213 project.

c. Analysis of Acceptability of Member Cooperators. Section 213 Sales Type Cooperatives involve single family dwellings built for release to members of the cooperative following completion of the entire project. It is necessary, therefore, to determine that each individual member meets HUD-FHA requirements from the standpoint of credit standing, ability to pay, motivating and monetary interest in the transaction, stability of employment and ability to make the required investment in the cooperative project. These determinations are made in accordance with Section 203(b) instructions. The Mortgage Credit Report, FHA Form 2900-2, will be completed for each member in accordance with outstanding instructions contained in Reference (7) of the Foreword.

(1) The term of the individual mortgage on the dwelling unit released from the blanket mortgage shall not exceed 30 years from the beginning of amortization or 35 years from such date, if the mortgagor is not able, as determined by the Assistant Secretary-FHA Commissioner, to meet the payments under a mortgage having a shorter amortization period.

(2) When analyzing the acceptability of member cooperators prior to closing, FHA Form 2900-2 is reviewed and the Rating of Mortgagor completed. Item 17, "Ratios", and Recommendations, are not completed until application for insurance of an individual mortgage on property to be released from the project mortgage is received. A notation should be made opposite each name in the appropriate column on the original copy of the Cooperative Membership Exhibit, FHA Form 3203, to indicate amount of cash available for investment (including earnest money deposit), monthly net effective income of the members, total housing expense for type of unit to be occupied, and the gross effective income.

(11-7) Under "Remarks" indicate which members, if any, do not meet requirements with respect to credit standing, ability to pay, stability of employment, and ability to make the required down payment. The duplicate copy of this exhibit will be completed in a similar manner by typing these items of information thereon, and will be sent to the Director, Office of Unsubsidized Insured Housing Programs, Attention of Cooperative and Condominium Housing Branch.

d. The Number of Members or persons agreeing to become members of the proposed mortgagor corporation must equal at least 100% of the total number of family units in the project, and all of these members or proposed members must be found acceptable from the standpoint of credit characteristics, ability to make their required down payment, stability of employment, and adequacy of effective income before approval of the mortgagor may be recommended.

e. Ability to Meet Investment. When analyzing the cooperative membership, all of the members or proposed members, in addition to all other requirements, must be found acceptable from the standpoint of their ability to make their required investment in the cooperative. The required investment is the difference between the total cost of acquisition and insurable mortgage amount. In no case shall the cooperative member's investment be less than the prescribed percentage of acquisition cost required under Section 203(b)(2). Investment requirement must also be satisfied without resorting to secondary financing.

(1) Analysis is made of the paying ability and credit standing of each member in order not only to determine acceptability of the group, but also in order to predetermine acceptability of the individual as mortgagor when his dwelling is released from the blanket mortgage, and the outstanding balance of the unit mortgage amount secured by his dwellings is reinsured under Section 213.

(2) Individuals who for any reason are considered unacceptable cannot be approved as members of the proposed mortgagor corporation. The Mortgage Credit Examiner prepares a schedule for the Director listing the names of individuals who do not qualify and indicating the reasons why they do not qualify as members. If, as the result of some

(11-7) rejections, the number of approved individuals is less than 100% of the total number of family units in the project, this schedule should also indicate the number of additional members to be obtained before approval of the mortgagor can be recommended.

f. Determination of Acceptability of Cooperative Organization.

After analysis of the credit acceptability of the individual members of the cooperative but before endorsement for insurance it must also be determined that the cooperative organization has the ability to close the transaction in a satisfactory manner. This involves estimating requirements for completion of the project by totaling amounts needed for on-site construction, land, off-site requirements and working capital. When the amount of the project mortgage is deducted from the foregoing, the resultant represents the equity requirement for the entire project. The amount of working capital held by the cooperative organization plus the total amount of additional cash available from the individual member must equal the total cash required over and above the mortgage proceeds. These determinations are made on FHA Form 2264A in accordance with instruction in Reference (3) of the Foreword.

g. Financial Requirements for Closing. The accumulation of the necessary data to provide the closing attorney with accurate financial details needed to close the mortgage transaction necessitates the initiation of direct inquiries to the cooperative organization. The information to be requested will include the amount of the construction contract, the contractor's fee, the architect's fee and the amount of contract for off-site improvements, if any. These figures will be subject to such modifications as are necessary to conform to the actual contracts and financial details agreed to at closing between the parties to the transaction. These data are required only in those cases involving the insurance of advances of mortgage proceeds and are recorded on FHA Form 2283-c in accordance with applicable instructions contained in Reference (3) of the Foreword.

h. Assurance of Completion. At the final initial closing of a Section 213 project involving the insurance of advances, a satisfactory assurance of completion must be provided in accordance with the HUD-FHA Regulations.

11-8. INSURANCE OF ADVANCES. Follow basic 207 instructions outlined in Reference (8) of the Foreword, except as modified herein.

a. Final Advance. The amount to be approved as final advance must be limited so that the total mortgage proceeds including the final 10% holdback cannot exceed the maximum insurable mortgage as determined at closing less the net decrease in replacement cost, if any, due to construction changes.

b. Revision Due to Construction Changes. Where the Valuation Section has found it necessary to revise the replacement cost and the estimate of value on the Valuation Report due to construction changes when the replacement cost of the individual properties are not affected proportionately, it will be necessary to redetermine unit mortgage amounts for the purpose of modifying the credit instrument with respect to the original release prices.

Determination of the revised unit mortgage amounts (original release prices) will be determined by preparing a memorandum form in accordance with the example I or II, Figure 1, and instructions that follow.

c. Replacement Costs. Where construction changes affected the replacement cost of the individual units proportionately and a net decrease in the replacement cost resulted, the unit mortgage amounts (original release prices) must be reduced in the same ratio that the total net decrease bears to the original mortgage amount and the credit instrument modified accordingly. The approval of the final advance should be conditioned upon adjusting the original release price and modification of the credit instrument in form approved by the Assistant Secretary-FHA Commissioner.

d. Adjustment of Unit Mortgage Amounts. When it has been determined that any or all of the unit mortgage amounts (original release price) must be adjusted, a memorandum is prepared to the Director listing the Identity Number, and the adjusted unit mortgage amounts of all individual units affected in order that they may obtain from the mortgagee the proper modification of the credit instrument prior to final endorsement thereof.

11-9. CONSTRUCTION CHANGES. Construction change procedure set forth in Reference (8) of the Foreword is applicable to the processing of requests for approval of changes for Section 213 projects except as follows:

(11-9) a. Requests for Consideration of Proposed Construction Changes will be initiated on FHA Form 2437 as in Section 207 projects. However, the provisions applicable to Section 213 Management and Sales Type on the reverse side of the form must be completed by the contractor and mortgagor. These provisions provide for the contractor to state if he agrees to assume any additional cost resulting from the proposed changes and for the mortgagor to indicate the amount of increase or decrease, if any, in the construction contract.

b. Increased Cost. When the provision indicates an increased cost to be paid by the mortgagor, a cash deposit is required as a condition for approval of the change. The amount of the deposit will be the difference between the increased amount of the construction contract and the original contract price except, when the HUD-FHA estimate indicates a net increase of $2500 or more, the amount to be deposited will be the amount of the HUD-FHA estimated net increase in cost or the amount of the increase in the contract amount, whichever is greater.

c. Figure 1 which follows exemplifies the processing necessary to carry out the above instructions.

11-10. INSURANCE OF INDIVIDUAL MORTGAGES.. Mortgages secured by individual single family dwellings released from a project mortgage on a sales type project can be insured individually under Section 213 only in connection with the release from the project mortgage. There is no provision for insurance of a subsequent or refinancing mortgage under Section 213 following termination of the original, individual contract for insurance. The commitment to insure the project mortgage provides for the issuance of a firm commitment to insure each individual property upon submission of an application for insurance under Section 213 within four months of the date of final endorsement.

a. The Mortgagor must be a member of the cooperative whose credit standings, cash investment and other qualifications have been approved by the Assistant Secretary-FHA Commissioner. An application for insurance of an individual mortgage received within the four months' period involving a mortgagor, who has been previously approved as a member of the cooperative, does not require redetermination of the acceptability of the borrower.

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(1) The previously prepared FHA Form 2900-2, Mortgage Credit Report, is adjusted to reflect amendments, if any, Item 17, "Ratios", and Recommendations are completed.

(2) The mortgage amount must not exceed the unpaid balance of the unit mortgage amount (original release price) or the amount which would be insurable under Section 203(b)(2) based on acquisition cost and must be in multiples of $50.

(3) The term of mortgage must not exceed 30 years, (35 years if the mortgagor is not able, as determined by the Assistant Secretary-FHA Commissioner, to meet the payments under a mortgage having a shorter amortization period), and must be for either 10, 15, 20, 25, or 30 years. (35 years in the above exceptional cases.)

b. Mortgage Credit Analysis and Procedure as follows is to be applied to applications for insurance of an individual mortgage under Section 213 upon release of the security from the project mortgage where:

(1) The members of the cooperative have not been previously approved in connection with the project mortgage although application is received within the four months' period, and

(2) Application for insurance is not received within the four months' period regardless of whether such member has been previously approved.

c. Application for Insurance Received Within Four Month Period. Applications for insurance of an individual mortgage covering a property to be released from the project mortgage involving a mortgagor who has not been previously approved as a member of the cooperative will be routed to the Mortgage Credit Section. The qualifications of the mortgagor will be determined in accordance with the instructions for the approval of a member of the cooperative in connection with the recommendation for the issuance of the commitment covering the project mortgage. A memorandum will be prepared recommending approval or rejection of the mortgagor as the case may be.

(1) Where approval is recommended, the mortgagor's effective income, Federal Income Tax and the net effective income should be listed. When recommending rejections, the

(11-10) reasons should be clearly stated and a letter to the mortgagee prepared for the Director's signature. A copy of the memorandum will be retained in the Credit Control Binder.

(2) In the cases involving the approval of a mortgagor in substitution for the original member, the name of the mortgagor should be written above the name of the original member on the Membership Exhibit, FHA Form 3203, and a line drawn through the name of the original member and the other entries where adjustments in the amounts are required in the various columns.

d. Application for Insurance not Received Within Four-Month Period. When application for insurance is not received within the four months' period, the following procedures are applicable. Applications of this procedure are predicated in part upon consideration of the fact that the new contract for insurance will be in substitution of the Assistant Secretary-FHA Commissioner's existing insurance liability under the Section 213 project mortgage.

Where it is the conclusion that insurance of the new mortgage will not be detrimental to the Assistant Secretary-FHA Commissioner's interest in view of the existing insurance liability, the Director is authorized by the Assistant Secretary-FHA Commissioner's findings in the new case, the Underwriting conclusions with respect to the property to be released from the project mortgage, provided these conclusions are supported by additional findings to establish that:

(1) Under reinspection the property is found to be a dwelling designed principally for a single-family residence.

(2) The terms and amount of the individual mortgage to be insured does not exceed a 30 year (35 years if the mortgagor is not able, as determined by the Assistant Secretary-FHA Commissioner, to meet the payment under a mortgage having a shorter amortization period) term, and the unpaid balance of the unit mortgage amount (original release price) under the project mortgage. The term must be either 10, 15, 20, or 30 years (or 35 years in

exceptional cases).

(11-10) (3) The mortgagor is acceptable under prescribed Underwriting requirements for Section 203(b)(2).

e. The Mortgage Credit Examiner. When an application of the type described herein is received the Mortgage Credit Examiner prepares the case for processing as follows:

(1) The Valuation Section is requested to make a special memorandum report to indicate:

(a) Whether the property upon reinspection is found to be a dwelling designed principally for a single-family residence;

(b) The nature and cost of repairs or replacements, if any, to repair damage as a result of fire, earthquake, flood, tornado, or waste;

(c) The nature and cost of other repairs and replacements, if any, necessary for the preservation of the property.

(2) Preliminary analysis of the application is made and required credit information is ordered in accordance with Underwriting instructions under Section 203.

(3) After receipt of the memorandum report from the Valuation Section and other necessary information the case is assigned for processing.

f. Mortgage Credit Analysis is undertaken in the same manner as for acceptance of a mortgagor under Section 203 except as noted below:

(1) If the property has been converted to a use which would make the new mortgage ineligible for insurance or if the mortgagor obviously is unacceptable, a memorandum recommendation to reject the application is made.

(2) In all other cases a Mortgage Credit Report, FHA Form 2900-2, is completed in accordance with outstanding instructions.

(11-10)g. Substitute Mortgagor. If a request for credit approval of a substitute mortgagor after insurance on an individually insured Section 213 mortgage is received, it will be processed under the procedure involving use of FHA Form 2210, Request for Credit Approval of Substitute Mortgagor. Following receipt of an application for approval of a substitute mortgagor, mortgage credit analysis is undertaken in the same manner as for approval of a substitute mortgagor under Section 203.