
CHAPTER 3. PROGRAM DESIGN AND OTHER REQUIREMENTS

3-1. PROGRAM DESIGN

The applicant shall develop its Urban Homesteading Program design in compliance with 24 CFR Part 590.7. The Program requirements include the following:

- A. Designation of Urban Homesteading Neighborhood; Coordinated Approach Toward Neighborhood Improvement. 590.7(a).

The applicant shall designate one or more neighborhoods which have available federally-owned properties to carry out its local urban homesteading program. With the exception of communities below 25,000 in population, target areas should not be approved that, either separately, or in combination, encompass all or substantially all of a community's total area. Exceptions to this standard may only be approved by the Director of the Urban Homesteading Program in Headquarters. Prior to submission of its application to HUD, the applicant shall develop a plan that provides for the improvement of these neighborhoods through the homesteading program and the general upgrading of community services and facilities, and through other measures needed to assure a suitable living environment, in combination with other public or private revitalization efforts affecting the neighborhood. At a minimum, the applicant must demonstrate that other activities, such as rehabilitation loans, water and sewer improvements, street and sidewalk improvements, and community and/or social services will support the efforts of the homesteading program.

- B. Minimum Number of Properties. 590.7(a).

An applicant should be reasonably certain that it will be able to acquire a minimum of five properties each fiscal year. Localities that will not be able to acquire five properties should not participate as a single entity, but should participate under the jurisdiction of a State or county program, or the umbrella of a single public agency or qualified community organization designated by several units of general local government to administer a program for more than one locality under separate Urban Homesteading Agreements with each unit of general local government.

- C. Selection and Management of Properties. 590.7(b)(1).

The applicant's program shall include procedures for selecting and acquiring one- to four-unit federally-owned properties suitable for homesteading, and for managing properties before conditional conveyance to homesteaders. This includes inspecting properties prior to taking title and assuming liability for injury or damage to persons or property due to a defect in the dwelling or its

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equipment, or for any other reason related to ownership of the property. Properties will remain unrepaired until conditionally conveyed to homesteaders. The LUHA shall, if feasible, continue to include properties in its master insurance coverage if homesteaders have difficulty obtaining coverage initially after conditional conveyance and prior to the property achieving a standard where private insurers will cover the homesteader's interest in the property.

- D. Designation of LUHA. 590.7(c).
1. Responsibilities. 590.7(c)(1). The applicant shall designate a LUHA, which shall have primary responsibility for administering the local urban homesteading program for the applicant. The LUHA shall be the legal entity that accepts title in its own name to federally owned properties conveyed by the applicable Federal agency with reimbursement from Section 810 funds and which conveys title to such properties to homesteaders pursuant to paragraph (b) of 24 CFR 590.7. Although the applicant may at any time amend its local urban homesteading program to designate a new LUHA, subject to HUD approval as described in Chapter 4, paragraphs 4-5 and 4-6, and 24 CFR 590.13-.15, neither the applicant nor the designated and approved LUHA may delegate or contract out to another legal entity, the function of accepting and conveying in its own name title to properties for homesteading purposes pursuant to 24 CFR Part 590. To the extent permitted by the applicant, the LUHA may use third parties as consultants, or agents to assist it in carrying out other functions and responsibilities with respect to the local urban homesteading program, by entering into a written agreement between the LUHA and the third party. No such agreement shall be deemed to relieve the LUHA or the applicant of responsibility for the third party's actions in conjunction with the local urban homesteading program.
 2. Identity of LUHA. 590.7(c)(2). The LUHA must have legal authority to carry out a local urban homesteading program as described in 24 CFR 590.7(c), including the authority to accept and convey title to properties pursuant to 24 CFR 590.7(b). To the extent consistent therewith, the applicant State or unit of general local government may:
 - a. act as LUHA in its own name, while identifying within its administrative organization a lead department or agency to act as the primary contact point for HUD, VA and FmHA (in such a case, the applicant itself is referred to as the LUHA);

- b. designate, and enter into a written agreement with, a legally separate public body or agency to act as LUHA in accordance with the following paragraph 3; or

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- c. designate, and enter into a written agreement with, a qualified community organization (as defined in Chapter 1, paragraph 1-4(K) and 590.7(c)(4)) to act as LUHA in accordance with the following paragraph 3.
3. Content of Agreement with Designated Public Agency or Qualified Community Organization. 590.7(c)(3). The applicant's written agreement with its designated public agency or qualified community organization shall contain at least the following provisions, and nothing inconsistent therewith:
 - a. the agreement of the LUHA to carry out the local urban homesteading program, including the acceptance and conveyance of title to properties for homesteading purposes, in accordance with the Act, 24 CFR Part 590, this Handbook, and the applicant's HUD-approved urban homesteading application;
 - b. the agreement of the LUHA to hold title (and the right of reverter or other interest retained after the conditional transfer to a homesteader under 24 CFR 590.7(b)(3)) to formerly federally owned properties conveyed to it pursuant to 24 CFR Part 590 in trust, solely for the purpose of conveying the properties to homesteaders (or for such alternative use as may be approved by HUD) pursuant to 24 CFR Part 590, and not to convey, encumber or otherwise deal with such property for its own benefit or account;
 - c. the agreement of the LUHA promptly to assign or convey title and/or other interests in properties held pursuant to 24 CFR Part 590 to the applicant, or to such new LUHA as may be designated by the applicant and approved by HUD, if the applicant terminates the LUHA's designation; and
 - d. the agreement of the applicant and the LUHA that the LUHA's designation shall not relieve the applicant of full responsibility to HUD for the conduct of the local urban homesteading program, and that HUD may take any corrective or remedial action pursuant to 24 CFR 590.31 against the applicant, the LUHA, or both, solely at HUD's option.

E. Affirmative Marketing. 590.11(d)(5)(ii).

The program shall include affirmative marketing practices that further national policy for fair housing by advertising the program in the media that will reach eligible persons least likely to apply for participation, and by otherwise marketing units in a manner to attract homesteaders regardless of sex, racial, or ethnic group. Such methods should include use of minority media outlets when

media advertising will be used to announce the availability of the program, and utilizing special outreach techniques/efforts to inform eligible persons who are not likely to apply without special outreach.

F. Homesteader Selection. 590.7(b)(2).

The program shall include equitable procedures for selecting homesteaders who have the capacity to make or cause to be made the repairs and improvements required under paragraph H below. The procedures shall:

1. exclude prospective homesteaders who own any other residential property. (This includes owners of mobile homes regardless of whether they own their land or rent space in a mobile park, holders of life estates, owners of condominiums, cooperatives, or property used for either investment or recreational purposes, i.e., a vacation house or a rental unit. It also excludes persons with a right to purchase properties utilizing a land contract.)
2. take into account the prospective homesteader's capacity to rehabilitate the property, including the ability to reduce rehabilitation costs through his/her own labor or other resources or contributions. The homesteader's capacity includes the ability to do some of the work, to manage the work of contractors, to obtain assistance from other sources, such as community organizations, and/or to obtain the funds required to finance the work. Though a LUHA is not required to give priority to applicants who can contribute their own skills and labor, those contributions which can be verified must be taken into account in assessing an individual homesteader's ability to make or cause to be made the necessary repairs.
3. provide that membership in, or other ties to, any private organization (including a qualified community organization) may not be made a factor affecting selection as a homesteader. Furthermore, membership of a potential homesteader in any private organization doing business with a qualified community organization, and any other ties to a

particular private organization, is not to be made a criterion For homesteader selection.

4. give a special priority to prospective homesteaders who are "lower income families" as defined in Section 3(b)(2) of the United States Housing Act of 1937, which includes single person households. Generally, this means that the family's annual income does not exceed 80% of the median income for the area, with adjustments for smaller and larger families. Permissible adjustments to income, and the median income for the area shall

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be determined in accordance with the requirements for the Section 8 Program in 24 CFR Part 813.

The special priority requires a LUHA to offer a Section 810 property to a qualified prospective homesteader who meets the "lower income" definition above before offering a property to any other prospective homesteader who does not qualify For the priority. An otherwise qualified priority prospective homesteader must also be credit-worthy, having the capability to secure the financing and manage the repayment of the debt associated with rehabilitation of a homesteading property. This could be determined initially through a credit check, and thereafter through the loan underwriting process.

To reduce the administrative burden due to an influx of applications, the LUHA in advertising its program and availability of properties should announce up front the selection criteria, thus assuring that most prospective homesteaders will meet the criteria. Also, the LUHA may charge an application fee, limited to the cost of a credit check. This fee generally shall not exceed \$25, unless the applicant does not subscribe to a credit bureau service, in which case, the fee may be more. The LUHA shall refund the application fee if it determines the prospective homesteader is ineligible prior to a credit check, e.g., under age to enter into a binding contract.

5. include locally adopted criteria reasonably matching the family size to the number of bedrooms in the property. Such criteria shall not permit homesteaders who are one-person households to be awarded a property having more than two bedrooms, unless there are no larger households on the waiting list.
6. specify other reasonable selection criteria, if any, which must be specified in the applicant's application. Other selection criteria may include preferences for the selection of neighborhood residents or other local residents only to

the extent that they are consistent with affirmative marketing objectives to which the LUHA certifies under 24 CFR 590.11(d)(5)(ii). Preferences may not be based on the length of time the prospective homesteader has resided in the jurisdiction or the neighborhood. In addition, persons who are working, or who have been notified that they are hired to work, in the jurisdiction shall be extended any preference available to current residents. (If there is a low-income applicant otherwise qualified to participate in the program, who does not meet the locally imposed residency criteria, then that applicant would still take precedence over any non-lower income applicant meeting the local residency criteria.)

Additional generally permissible selection criteria may include preference for those displaced due to other public action, minimum income limits to assure ability to repay a rehabilitation loan, maximum income limits to assure that "lower income families" are being served, or physical handicap. All selection criteria must be submitted to and approved by Field Office staff in accordance with 24 CFR 590.11(a) and 590.13. (See Chapter 4, paragraph 4-2, C.4.)

7. Assure nondiscrimination upon the basis of race, creed, color, sex, national origin, age, handicap, religion, or familial status in the selection of homesteaders.

G. Conditional Conveyance. 590.7(b)(3).

The program shall provide for the conditional conveyance of unoccupied, unrepaired residential property to homesteaders within 1 year, or loss, of title transfer to the LUHA. Property received from the Federally-owned inventory shall be conditionally conveyed without substantial consideration. The term "without substantial consideration" is defined as a nominal amount not exceeding the minimum local definition of "consideration" used to transfer real property, generally \$1.00.

"Conditional conveyance", as used here and in 24 CFR 590.7(b)(3), does not necessarily require that the homesteader immediately receive an interest technically classified as a real property interest under applicable State law. If the document contains a contractual right to acquire fee simple title when the homesteader has complied with all of its terms and with the homesteader agreement, that is sufficient for this purpose.

While a LUHA is restricted to the transfer of a property for nominal consideration, the LUHA may require a homesteader to pay for items such as recording fees, transfer taxes and property taxes after acquisition to the extent that such fees and taxes

are uniformly applicable to other purchasers of property in the jurisdiction. Furthermore, the homesteader can be required to pay third parties, but not the LUHA or other public agencies, for all of the costs that would normally be incurred in connection with the rehabilitation of the property. This includes, but is not limited to, architectural and inspection fees and costs associated with arranging private rehabilitation financing (if applicable), such as appraisal fees, points, loan origination fees, and closing fees. Where a loan is made directly to a homesteader by the applicant or the LUHA, it is assumed that applicant or LUHA staff or other public or nonprofit staff, will perform these functions; and, therefore, the costs thereof are not to be charged to the homesteader. The homesteader is responsible for payment of the loan principal, plus interest, if any. The LUHA may not pass on to

the homesteader any property management expenses and taxes that it incurs while the property is in its inventory prior to conveyance to the homesteader. Any charges should be clearly distinguishable from the nominal consideration for the property.

The LUHA will include in each deed conveying a property, if applicable, a covenant enforceable under applicable State law, prohibiting the homesteader, or any successor homesteader, from discriminating on the grounds of race, creed, color, sex, national origin, age or handicap in the sale or rental of the property.

- H. Homesteader Agreement. 590.7(b)(5). The program shall provide for executing, concurrent with or as a part of the conditional conveyance, a Homesteader Agreement between the LUHA and the homesteader which shall require the homesteader to:
1. repair health and safety defects within one year. The agreement must provide that any defects that pose a substantial danger to health and safety will be repaired within one year from the date of conditional conveyance of the property. For purposes of this requirement, States and localities have reasonable discretion in determining what poses a substantial danger to health and safety both to the prospective homesteader and to the community. Any defect that poses such a hazard must be repaired within one year. It should be noted that any repairs financed through the Section 312 Program must also comply with its loan terms. While rehabilitation activity under Section 312 must, under HUD policy, be completed within 24 months, the loan note usually specifies a period not to exceed six months. In general, a homesteader agreement may require that rehabilitation be completed in a shorter time frame than one year unless the shorter term unreasonably impairs the

homesteader's ability to utilize self-help in the rehabilitation process where he or she is qualified and willing to do so. Further, States and local governments may enforce generally applicable requirements relating to occupancy of homesteading properties, like any other housing under their jurisdiction.

2. complete all repairs within three years. The agreement must provide that all additional repairs and improvements necessary to meet the applicable local standards for decent, safe and sanitary housing, and any energy conservation measures designated by the LUHA will be completed within three years from the date of conditional conveyance of the property to the homesteader. Again, this is a maximum permissible period; the homesteader agreement may provide a shorter period where warranted.

3. Occupy the property for five years. The homesteader must agree to occupy the property as his/her principal residence for not less than five consecutive years from the date of initial occupancy. A LUHA shall assure that the date of initial (physical) occupancy is recorded, since the date of the occupancy permit or the date of occupancy projected in the Homesteader Agreement may differ from the date of actual occupancy.

Where a Section 312 loan exists on a homestead property, the LUHA shall assure that the Homesteader Agreement and/or the operative document, i.e., certificate of occupancy, that establishes the actual date of occupancy is submitted to the Section 312 loan servicer for inclusion in the homesteader's loan file. This is necessary in the event the homesteader defaults on the loan prior to the end of the 5-year period, so that the loan servicer will know to contact the LUHA to either work things out with the homesteader or to find a successor homesteader to assume the loan. (See paragraph 3-3.)

The five-year occupancy requirement may be determined infeasible and relief may be granted by HUD on a case by case basis in certain emergency situations. The following are examples under which relief may be granted:

- a. the property may have been made uninhabitable as a result of natural disaster or casualty loss;
- b. the property may have been taken by eminent domain;
- c. the homesteader's job may have been transferred outside of reasonable commuting distance of the property;

- d. the homesteader may have been determined to be mentally incompetent and removed from the property;
- e. the homesteader may have a terminal illness in which death is known to be imminent or the homesteader may have died.

Written requests for relief received from the LUHA will be approved or disapproved by the Field Office after consultation with the Headquarters Urban Homesteading Program Team on a case-by-case basis.

- 4. Permit inspections. The homesteader must agree to permit reasonable inspections at reasonable times by employees or designated agents of the LUHA to determine compliance with the Homesteader Agreement, including a yearly inspection to verify occupancy by the homesteader.

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- 5. Surrender possession of the property upon material breach of the agreement. The homesteader must agree to surrender possession of (vacate), and any interest in, the property upon any material breach of the Homesteader Agreement (including default on any rehabilitation financing secured by the property -- See paragraph 3-3), as determined by the LUHA.
- I. Monitoring and Selecting Successor Homesteaders. 590.7(b)(6). The program shall provide for monitoring of the homesteader's compliance with the Homesteader Agreement; revocation of the conditional conveyance and Homesteader Agreement upon any material breach by the homesteader; and, to the extent necessary and practical, selection of one or more successor homesteaders to assume the responsibility for homesteading the property including any existing debt for costs of rehabilitation. The LUHA shall make reasonable efforts to assure that the proposed successor homesteader assumes any Section 312 loan on the property subject to HUD approval of the terms of the assumption. Priority must be given to lower income families. If there are no priority applicants available who are willing or able to assume a Section 312 loan, HUD Headquarters may approve an exception to the requirement that assumptors of 3% Section 312 loans be lower income families in order to let a family above 80% of median income assume the loan. If a successor homesteader is selected, the homesteader shall execute a new Homesteader Agreement and the property shall be conditionally conveyed for a new five-year period, except that HUD may approve a lesser occupancy period to facilitate assumption of a Section 312 loan or any other type of financing on a homestead property. This lesser period cannot be

less than the greater of (1) two additional years, or (2) the remaining amount of the original occupancy period.

- J. Fee Simple Title. 590.7(b)(7). The program shall provide for the conveyance of fee simple title to the property from the LUHA to the homesteader, without consideration, upon compliance with the terms of the Homesteader Agreement and conditional conveyance. This occurs upon completion of rehabilitation and the five-year residency requirement.
- K. Homesteading Infeasible; Alternative Use. 590.7(b)(8). If homesteading of a federally-owned property after acquisition by the LUHA proves to be infeasible in the judgment of HUD, the LUHA shall not demolish, dispose of, rent or otherwise convert the property to its own use until the Field Office has approved an alternative use of the property consistent with the coordinated approach to neighborhood improvement. (See Chapter 10, Alternative Uses of Federally-Conveyed Urban Homesteading Property.)

3-2. CONFLICT OF INTEREST

The Urban Homesteading conflict of interest exclusion is intended to avoid any appearance of unfairness in the conduct of the program.

The exclusion applies to the individuals listed below and to those with whom they have family or business relationships. The period of coverage is during their current tenure and one year thereafter.

A. Persons not Eligible

- 1. No person shall be awarded an Urban Homesteading property, or receive a personal or financial interest or benefit from the award or rehabilitation of an Urban Homesteading property, or have any interest in any contract, subcontract or agreement with respect thereto, or the proceeds thereunder, if that person is:
 - a. an elected or appointed official or officer of the applicant;
 - b. an elected or appointed official or officer of the public agency or qualified community organization designated as the Local Urban Homesteading Agency (LUHA); or
 - c. an employee, agent, contractor, or consultant of the applicant or public agency or qualified community organization designated as the LUHA who:

- (1) exercises or has exercised any functions or responsibilities in connection with the administration of the Urban Homesteading Program, or assists or has assisted with rehabilitation activities, or
- (2) is in a position to participate in a decision making process or gain inside information with regard to such activities.

B. Exceptions

1. Threshold requirements

Upon the written request of the applicant, HUD may grant an exception to this exclusion on a case-by-case basis when it determines, using the factors listed in paragraph C. below, that such an exception will serve to further the purposes of the Urban Homesteading Program. An exception may be considered only after the applicant has provided the following:

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- a. a disclosure of the nature of the conflict, accompanied by an assurance that there has been public disclosure of the conflict and a description of how the public disclosure was made; and
- b. an opinion of the applicant's attorney that the interest for which the exception is sought would not violate State or local law.

C. Factors to be considered for exceptions

In determining whether to grant a requested exception after the applicant has satisfactorily met the threshold requirements listed above, HUD shall consider the cumulative effect of the following factors, where applicable:

1. whether the exception would provide significant benefit to the program or project which would otherwise not be available;
2. whether an opportunity was provided for open competitive bidding or negotiation;
3. whether the person affected is a member of a group or class of lower income persons intended to be the primary beneficiaries of the assisted activity, and the exception will permit such person to receive generally the same

interests or benefits as are being made available or provided to the group or class;

4. whether the affected person has withdrawn from his or her functions or responsibilities, or the decision making process with respect to the specific assisted activity in question;
5. whether the interest or benefit was present before the affected person was in a position as described under "Persons not Eligible;"
6. whether undue hardship will result either to the recipient or the person affected when weighed against the public interest served by avoiding the prohibited conflict; and
7. any other relevant considerations.

3-3. FINANCING MECHANISMS FOR URBAN HOMESTEADING PROPERTIES 590.7(b)(4).

The program shall provide procedures for the LUHA to undertake, or assist the homesteader in arranging, financing for rehabilitation required under the Homesteader Agreement. This requires the LUHA to assist the homesteader in securing financing or, if it chooses to provide financing for the rehabilitation required under the Homesteader Agreement.

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A. Section 312 Loan Program

If financing is through the Section 312 Loan Program, the LUHA shall assist HUD in monitoring and securing compliance with the terms of the loan during the homesteader's conditional title period, including securing an assumptor for the Section 312 loan, subject to HUD approval, in order to obtain a successor homesteader after the breach of the homesteader agreement or the Section 312 loan documents by the original homesteader.

1. Language to include in Homesteader Agreements. See Section 312 Rehabilitation Loan Program Handbook, HUD 7375.01 REV-2, paragraph 12-16(b). In order to avoid the possibility of a homesteader becoming entitled to full fee simple title to a homesteading property when he or she is not repaying a Section 312 loan, the Local Urban Homesteading Agency should include substantially the following language in each Homesteader Agreement involving Section 312 rehabilitation financing:

"The homesteader agrees that a default under the promissory note, the rehabilitation loan agreement, or the mortgage (deed of trust) evidencing any Section 312 loan obtained to finance the rehabilitation of the

homestead property shall constitute a default under this Urban Homesteader Agreement. This entitles the Local Urban Homesteading Agency to enforce any and all remedies available for a material breach or default under this agreement, including forfeiture of the homesteader's interest in the property. Specifically, the homesteader shall have no right to a final conveyance of the homesteading agency's reversionary interest in the property unless the homesteader is current on his or her Section 312 loan."

2. Loan Delinquency. If a Section 312 loan on a homestead property becomes delinquent, the following will occur:
 - a. After 30 days. The Section 312 master servicer will send a letter to the homesteader and the LUHA, and request the LUHA to begin proceedings to obtain a voluntary settlement or to exercise its reversionary interest. Upon receipt of this notice, the LUHA must contact the homesteader by letter, telephone, or personal visit to relate the importance of prompt payment and to remind the homesteader that non-payment constitutes a breach of the Homesteader Agreement, thus resulting in forfeiture of the property if neglected. The LUHA's collection efforts must be reported to the Section 312 master servicer at (800) 876-5626.

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- b. After 60 and 90 days. The master servicer will send a letter to the homesteader after 60 days to accelerate the loan and again request the LUHA to obtain a voluntary settlement or to exercise its reversionary interest. A letter will also be sent to the homesteader and LUHA after 90 days, at which time the LUHA should have already taken action to evict the homesteader.
3. Actions of LUHA to Obtain Voluntary Transfer of Property and Assumption of Section 312 Loan. A default on a Section 312 loan in and of itself constitutes a breach of the Homesteader Agreement, if the agreement contains the provisions required in paragraph 12-16(b) of the Section 312 Handbook as cited above. When a breach cannot be resolved, the homesteader must surrender all interest in the property and must vacate the property and the LUHA must attempt to re-homestead the property. When the reversionary interest is exercised by the LUHA, the security interest of the Section 312 loan executed by the homesteader will be cut off for HUD, but the original homesteader remains responsible for repayment of the loan. In this situation, HUD may seek a judgment as a recourse to collect the loan. The possibility of such action may serve

as an inducement to the Section 810/312 homesteader to agree to a voluntary transfer, and is an action which should be presented to a homesteader who is in default.

The LUHA should attempt to persuade the original homesteader in default to voluntarily transfer his or her interest in the property and the liability of the loan to a new homesteader by:

- a. offering the original homesteader a general release of liability on the Section 312 loan (prepared by HUD Field Counsel or the master servicer for approval by the Office of Urban Rehabilitation); and
 - b. agreeing that the homesteader's credit record and future eligibility for other HUD programs will not be affected.
4. Finding Successor Homesteader. As an aid to finding a successor homesteader who can afford the property, HUD may consider:
- a. a reduction in the principal amount of the Section 312 loan (and consequent reduction in the monthly payments) in cases where the appraised value of the property is less than the amount of the loan. If the original outstanding principal balance exceeds \$20,000, the Federal Claims Collection Standards (4 CFR 101-105) requires Justice Department Concurrence, as a "compromise" of the loan obligation.

- b. a write off of accrued interest.

Arrangements to obtain a current appraisal must be discussed with Headquarters Section 312 staff.

Where there is a voluntary transfer and assumption of the Section 312 loan, the successor homesteader must acquire the conditional title from the original homesteader, sign a new or modified Homesteader Agreement with the LUHA (which incorporates a new 5-year continuous occupancy period), and assume the Section 312 loan under the existing documents, or under modified documents, as appropriate. The LUHA is responsible for the preparation of homesteader and Section 312 loan documents; however, any modification to Section 312 loan documents must be cleared by HUD Field Counsel.

Any proposed assumption must be cleared with the Section 312 Rehabilitation Management Specialist/Urban Homesteading Coordinator before the property is

transferred to a successor homesteader. A copy of the new Homesteader Agreement should accompany the 312 loan assumption documents submitted to HUD. If a reduction or write-off of any part of a Section 312 debt is anticipated, it must be coordinated with Headquarters Section 312 staff and the master servicer.

5. Exercising the Reversionary Interest. If a homesteader resists a voluntary surrender of possession and transfer of the property to a successor homesteader, the LUHA must take steps to exercise its reversionary interest (or the equivalent), to evict the original homesteader, to protect the property from vandalism, and to find a successor homesteader to assume the loan.

The LUHA's recapture of possession and/or title to the property may wipe out HUD's security interest for the Section 312 loan, but it will not wipe out the loan itself. The loan, however, cannot be assumed by a successor homesteader without the consent of the original homesteader. The LUHA may facilitate an assumption by requiring all homesteaders to execute an irrevocable power of attorney at the time of conditional conveyance and the signing of the Section 312 loan documents, which would give the LUHA consent in advance to transfer the Section 312 loan to a successor homesteader in the event of a breach of the homesteader agreement. Without such a document, there can be no voluntary assumption of the Section 312 loan and the original homesteader continues to remain liable for payment. If a successor homesteader assumes the Section 312 loan after the LUHA exercises its reversionary interest, the

terms of the assumption and procedures noted in (b) above should be followed, except that the successor homesteader acquires the property from the LUHA instead of the original homesteader.

6. Foreclosure. Foreclosure or a deed in lieu of foreclosure divests the original homesteader of his or her right to owner occupancy of the property, also breaching his or her conditional title and Homesteader Agreement. Therefore, in foreclosing, HUD acquires only a partial interest in the property which is essentially worthless, unless it is merged with the reversionary interest held by the LUHA. A foreclosure also wipes out the Section 312 loan.

Therefore, a foreclosure or deed-in-lieu is a viable option for homesteading properties prior to conveyance of fee simple title to the homesteader only under the following

circumstances.

- a. The property has substantial net value over and above the estimated cost of foreclosure, superior liens, and property management expenses;
- b. The LUHA has first used all reasonable efforts to arrange a voluntary settlement with the original homesteader, in order to transfer the property to a successor homesteader who will assume all or a substantial portion of the Section 312 loan, which also both preserves the property for homesteading and minimizes the Government's Section 312 loss;
- c. The LUHA quit claims its interest in the property to HUD prior to the initiation of foreclosure (or acceptance by HUD of a deed-in-lieu) so that HUD acquires an interest it can dispose of; and
- d. The LUHA also agrees not to reclaim the property from HUD's inventory for re-homesteading.

If the property has substantial net value and the LUHA does not cooperate with respect to items 2, 3, and 4 above, HUD will view the LUHA as causing unnecessary losses to the Section 312 revolving fund and the Section 810 appropriation, and will consider terminating the LUHA's participation in these programs.

7. Tax Consequences Involving Loan Delinquencies.

- a. The LUHA must report to the IRS on Form 1099-S any gross proceeds of sale of a homestead/Section 312 security property (including the amount of the loan assumed) from a

voluntary conveyance or through exercise of the reverter clause.

- b. HUD Headquarters must report to the IRS on Form 1099-G the amount of principal reduction or accrued interest forgiveness in connection with a compromise.
- c. HUD Headquarters must report to the IRS on Form 1099-A when a Section 312 loan is foreclosed by HUD, a deed-in-lieu is accepted by HUD, or the security property is abandoned by the homesteader.
- d. The Field Office Section 312/Urban Homesteading

Coordinator must inform Headquarters when the circumstances in Items 2 and 3 occur so that the forms so noted can be filed.

B. Other public or private financing.

Where the rehabilitation is financed for a homesteading property with other public funding, such as CDBG funds, the LUHA should consider including language similar to that in paragraph 3-3 A.1. of this Handbook, in the Homesteader Agreement and/or the conditional conveyance instruments. The LUHA's homesteading interest may not be subordinated to a lien securing other public financing.

If a private lender is involved, HUD recommends that the LUHA negotiate with the lender a separate agreement wherein the lender will provide notification to the LUHA of any delinquency or default prior to any formal action; that the LUHA will be provided a reasonable period of time in which to exercise its reversionary rights, including action to remove the homesteader from the property, if necessary; and the LUHA can find a replacement homesteader to assume the existing obligation. Where private lenders are involved, the LUHA may find it necessary to make payments to keep the loan current until the successor homesteader is located. CDBG funds may not be used to make such loan payments unless there was a legally binding commitment to do so (such as a loan guarantee) prior to commencement of rehabilitation.

3-4. OTHER REQUIREMENTS.

A. Annual Inspection

The LUHA must verify by an on-sight inspection on an annual basis, the continued occupancy of the homestead property by the homesteader during the 5-year conditional period.

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B. Flood Disaster Protection Act (42 USC Section 4012a; 4106)

Buildings located within special flood hazard areas identified by the Federal Emergency Management Agency under the National Flood Insurance Program (NFIP) are subject to the Act and implementing regulations. The two requirements affecting homesteading properties are:

1. Either the LUHA as the initial owner or the homesteader as the ultimate owner must:
 - a. purchase flood insurance coverage (see paragraph 3

below);

- b. renew the coverage so that the flood insurance policy does not lapse during the mandatory period (see paragraph 5 below); and
 - c. provide proof of purchase of insurance to the HUD Urban Homesteading Coordinator if HUD is transferring the property to the LUHA, or to the LUHA if the LUHA is transferring the property to the homesteader -- for inclusion in the homesteading file.
2. The unit of general local government's responsibility is:
 - a. to establish and maintain its eligibility as a participant in the NFIP; otherwise homesteading is prohibited for buildings located in special flood hazard areas by Section 202(a) of the Act; and
 - b. to assure compliance with Section 102(a), which prohibits homesteading in a special flood hazard area, unless the property is covered by flood insurance.
 3. The LUHA must check property locations against NFIP flood maps to determine whether properties to be transferred are located within Flood Hazard Zones "A" and "V" series and for which flood insurance is required.
 4. Premium. Flood insurance coverage must be in the amount at least equal to the property value (less estimated land value) or to the maximum limit of coverage available with respect to the particular type of property as set forth under the Act, whichever is less.
 5. Term. The mandatory period for flood insurance is for the useful life of the property. The NFIP will assure compliance by providing an annual notification to HUD for any property transferred to the LUHA, but not yet transferred to a homesteader, and to the LUHA for any property transferred to a

homesteader. In completing the flood insurance application form, the LUHA or homesteader, as appropriate, will indicate the name and address of the monitor (HUD or the LUHA), in item #6 or #7 on the Federal Emergency Management Agency (FEMA) Form 81-16 or comparable form authorized by FEMA. Thereafter, FEMA will forward to the monitor (HUD or the LUHA) the insurance renewal premium notice and the national flood insurance expiration reissue premium notice in the same

manner as it does to the insured (the LUHA or the homesteader). Samples of these forms are contained as Exhibits 12-1 through 12-4 of HUD Handbook 7375.01, Rev. 2, Section 312 Rehabilitation Loan Program. The LUHA should keep an up-to-date listing of each insured property, including address, description, amount and the mandatory period of insurance coverage, the expiration and renewal dates of the flood insurance policy, the name and address of the insurer, and the applicable insurance policy numbers; and take any reasonable means to enforce the legal requirements and consult with the HUD Field Office promptly on any unresolved flood insurance purchase problem or delinquency.

C. Lead-Based Paint

Pursuant to 24 CFR section 590.11(d)(6), the Department's regulations with respect to lead-based paint at 24 CFR Part 35 are currently applicable to the Urban Homesteading Program. Part 35 contains the following relevant provisions:

1. Requirement of notification to "purchasers" of housing constructed prior to 1978 of the hazards of lead-based paint poisoning (Part 35, Subpart A). Although homesteaders are not technically "purchasers," the LUHA should nevertheless do this notification before a prospective homesteader accepts title to the property, as part of the process of informing the prospective homesteader about the results of the inspection and what rehabilitation is required to correct "immediate hazards" on "applicable surfaces" under Part 35, Subpart C. Thus, the homesteader will be in a position to accept title knowing what rehabilitation is required to meet lead-based paint hazard elimination standards.
2. Prohibition of the use of lead-based paint in federally assisted rehabilitation (Part 35, Subpart 8).
3. Provision requiring the inspection of housing constructed prior to 1973 and its treatment to eliminate "immediate hazards" on "applicable surfaces" (Part 35, Subpart C). Under Part 35, this consists principally of the covering or removal of defective paint surfaces, defined as cracking, scaling, peeling, chipping or loose paint. These conditions shall be

eliminated as part of the rehabilitation undertaken by the homesteader under the direction of the LUHA.

Some housing transferred to LUHAs may have already been treated by HUD to eliminate lead-based paint hazards as part of HUD's property disposition process; notification of hazards is still

required for these properties. In addition, if the property is being rehabilitated with either CDBG or Section 312 funds, more stringent hazard elimination requirements will apply (CDBG -- see 24 CFR section 570.608; Section 312 -- see 24 CFR section 510.410). Finally, Section 566 of the Housing and Community Development Act of 1987 substantially amends the Lead-Based Paint Poisoning Prevention Act, essentially to require testing of HUD-associated housing constructed or substantially rehabilitated prior to 1978, and treatment of both intact and non-intact paint surfaces. LUHAs shall comply with HUD's regulations implementing the new act with respect to all properties transferred to homesteaders.