

Form FHA 021-4

UNITED STATES DEPARTMENT OF AGRICULTURE
RURAL DEVELOPMENT
HARRISBURG, PENNSYLVANIA

TO:
State Office
Area Office

STATE PROCEDURE
NOTICE

ISSUE NO. 323

DATE: April 05, 2011

RURAL DEVELOPMENT MANUAL CHANGE

The purpose of this Procedure Notice is to supplement RD Instruction 1927-B, paragraph 1927.51, 1927.55 (f), 1927.57 (d) and provide further guidance on primarily three (3) issues:

1. In some cases, not all of the rights to the property are conveyed to the buyer as part of the sale. Guidance is provided for the loan approval official to determine if listed title exceptions are acceptable to the Agency.
2. Form RHS PA 1927-8 will be completed on all single Family Housing Direct loans where a lien with priority over the Rural Development mortgage will remain against the real property securing the RHS loan (s).
3. For existing Section 502 DIRECT borrowers, sample letters are provided for the following situations involving mineral leases:

RD notified AFTER mineral lease is executed:

Letter #1- Notification to Leasing Company-cannot execute Consent of Lien holder Form

Letter #2-Notification to Borrower to contact CSC

RD notified BEFORE mineral lease is executed:

Letter #3-Notification to Borrower-documentation needed for Agency to consider consent to lease

REMOVE: PA PN 317 (1927-B), dated July 14, 2010 (filed behind RD Instruction 1927-B)

INSERT: PA PN 323 (1927-B), dated April 05, 2011 as a State Supplement behind RD Instruction 1927-B.

Title Clearance and Loan Closing

This State Instruction supplements the following section of RD Instruction 1927-B.
1927.51 General

(a) Types of loans covered by this subpart. This subpart sets forth the authorities, policies, and procedures for real estate title clearance and closing of loans, assumptions, voluntary conveyances and credit sales in connection with the following types of Rural Housing Service Loans: Rural Housing (Single Family Housing), Farm Labor Housing (LH), Rural Rental Housing (Multi-family Housing), Rural Cooperative Housing (RCH), and Non-Program (NP) loans. This subpart does **NOT** apply to guaranteed loans.

1927.55 (f) Approval Official's responsibilities after receipt of a preliminary title opinion or title insurance binder

The loan approval official will review the preliminary title insurance binder to determine if listed exceptions are acceptable to the Agency. As stated in Handbook 1-3550, Chapter 8, Section 8.6 (B), the Loan Originator needs to review exceptions to determine if the exception will adversely affect the property's title, suitability, or security value.

Mineral Leases and Outstanding Mineral Rights

In some cases, not all of the rights to the property are conveyed to the buyer as part of the sale. Certain property rights may have been transferred to someone else by the current owner or a prior owner and, therefore, these rights cannot be transferred to the current buyer. In this example, these rights are considered to be excepted from the transaction. Buyers are strongly encouraged to have oil, gas, and mineral rights leases reviewed by an Attorney with expertise in this area of the law.

(i) If any mineral leases are listed as exceptions in the commitment and if these leases have expired because of non-production or non-payment of delay rentals, the approval official must have these exceptions removed, if possible. An affidavit of non-production and/or non-payment of delay rentals on a form acceptable to the title insurance company and signed by the lessee may accomplish this purpose. Any such affidavits or similar forms used must be recorded at the borrower's expense.

(ii) If there are any outstanding mineral rights and unexpired leases, it is the policy of the agency to require that the owners of these rights and leases waive the right to use the surface of the security property for exploration, drilling and/or mining operations, production, transportation and storage and to agree not to disturb the surface of the security property in the exercise of their rights. If a waiver of surface use cannot be obtained, the agency has two options: (a) find another site; or (b) waive the title exception. Rural Development Loan Approval Officials have the authority to grant a waiver to this title exception when the granting of the waiver is necessary

to facilitate the loan closing and the agency's security position will not be substantially at risk of suffering from possible damage or devaluation due to mineral exploration and production.

If the Rural Development Loan Approval Official elects to waive a mineral title exception, the agency may be able to limit the damage to the surface which would be caused by the exercise of an outstanding mineral rights and rights under unexpired leases by obtaining PA Endorsement 1030, "Restrictions, Encroachments, Mineral Endorsement". It is not the agency's policy to require this endorsement in every case where a waiver of the right to use the surface cannot be obtained and where the Loan Approval Official is waiving the mineral title exception. The Loan Approval Official should, however, consider requiring this endorsement if there is a risk of mineral exploration in the area and if the Loan Approval Official has elected to waive the mineral title exception.

Other Exceptions: Other exceptions to title may appear in the commitment. All exceptions should be removed, if possible, and the Loan Approval Official should work with the title insurance company to see what is needed to remove those exceptions.

1927.57 (d) (5) Form RHS PA 1927-8 "Agreement with Prior Lien Holder"

Form RHS PA 1927-8 will be completed on all single family housing loans where a lien (other than Rural Development liens or tax liens to local governmental authorities) with priority over Rural Development's mortgage will remain against the real property securing the RHS loan (s).

No later than closing, Form RHS PA 1927-8 will be executed and notarized. A copy of the form will be filed in position 5 of the borrower's docket and a copy will be provided to the prior lien holder.

Borrower Actions Requiring RHS Approval

In accordance with RD regulations found at 7 CFR 3550.159 (a), borrowers must obtain Agency authorization before leasing mineral rights on their security property. Borrowers acknowledge this requirement by executing an Application Orientation Guide, Form RD 3550-23 prior to loan closing.

The attached Sample Letter # 1 and #2 can be used to notify the Leasing Company and the Borrower respectively; in those cases where Agency approval was not obtained PRIOR to the execution of the lease.

The attached Sample Letter #3 can be used to notify the Borrower of documentation which needs to be submitted to the Agency, so that a determination can be made if the PROPOSED lease is in the best interest of the borrower and the government.

United States Department Of Agriculture
Rural Housing Service
Agreement With Prior Lien Holder

WHEREAS, _____ (Originating Lender), hereinafter "Mortgagee" is (or is about to become) the holder of a certain mortgage, in the principal amount of \$_____ which has been (or will be) recorded in the Office of the Recorder of Deeds of _____ County, Pennsylvania, which mortgage is (or will be) a first lien against the following property, described therein, which has been (or is about to be) purchased by _____ hereinafter "Mortgagor(s)" at the following **PROPERTY ADDRESS:** _____ and _____

WHEREAS, Mortgagor(s) also has/have been approved for a loan by the United States of America, acting through the Administrator of the Rural Housing Service, hereinafter the "Government", for the purpose of improving or purchasing and improving the real estate, which is (or will be) secured by a Mortgage or other security instrument that will be subject to the mortgage held by Mortgagee referred to above.

NOW THEREFORE, in consideration of the insuring and/or making of the loan by the Government, Mortgagee, for itself, its successors and assigns does hereby agree as follows:

1. Mortgagee will not declare the mortgage to be in default, and the indebtedness secured thereby will not be accelerated unless at least thirty (30) days prior written notice thereof has been provided to the State Director of Rural Development, by Certified Mail, return receipt requested at the following address: Suite 330, One Credit Union Place, Harrisburg, PA 17110-2996.
2. The Government may, at its option, cure any monetary default by paying the amount of the borrower's delinquent payments (including late charges) to the Mortgagee.
3. Should the Government take legal action to acquire the real estate described above, the Mortgagee will not declare its mortgage to be in default for any non-monetary reason for eighteen (18) months from the date of acquisition by the Government, in order to allow the Government the opportunity to find a purchaser for the real estate, and the Mortgagee will cooperate with the Government in attempting to arrange for an assumption of the first mortgage debt to a qualified purchaser.
4. That to the extent the prior lien secures future advances which would have priority over the Government's security instrument, no advances for purposes other than taxes and insurance, will be made under any future advance feature of the mortgagee's security instrument without the written consent of the State Director of Rural Development.

5. If the first mortgage instrument prohibits a junior lien or mortgage without Mortgagee's consent, this agreement constitutes the Mortgagee's consent to the Government's mortgage lien.

6. In the event that Mortgagee forecloses on its mortgage, Mortgagee agrees to limit its attorney fees to no more, than what is customary for the area, for this type of Real Estate Mortgage.

IN WITNESS WHEREOF this agreement has been executed by Mortgagee this _____ day of _____, 20__.

BY: _____

TITLE: _____

ACKNOWLEDGMENT

STATE OF PENNSYLVANIA)
COUNTY OF _____) ss:

I, the undersigned Notary Public in and for said State and County do hereby certify that on the ____ day of _____, 20__, before me personally appeared _____, known to me and to me known to be the person who executed the foregoing instrument, and he/she acknowledged to me that as his/her free act and deed, he/she executed the said instrument in the capacity therein stated and for the purposes therein contained.

In witness whereof, hereunto set my hand and official seal.

NOTARIAL
SEAL

NOTARY PUBLIC

My commission expires: _____

SAMPLE RESPOSE TO OIL / GAS LEASING COMPANY (EXISITING LEASE)

DATE

ABC Oil & Gas Corporation
P.O. Box
Any town, PA 12345

RE: Notification of Oil & Gas Lease
Mr. and Mrs. Robert Smith
Property Address: 100 Main Street, Rural, PA 19999

Dear Sir or Madam:

This is in response to your letter dated March 1, 2011, regarding your Notification of Oil & Gas Lease for the property owned by Mr. and Mrs. Smith located at 100 Main Street, Rural, PA 19999. USDA Rural Development currently holds a mortgage on this property.

Please be advised that we cannot execute your "Consent of Lien Holder" form. In accordance with Rural Development regulations found at 7 CFR 3550.159 (a), borrowers must obtain Agency authorization before leasing mineral rights on their security property. In this case, the subject borrower executed a lease with ABC Oil & Gas Corporation on September 20, 2010 and the "Consent of Lien Holder" is being requested now, six (6) months later.

In addition, please be advised that qualified housing borrower's may be receiving a payment subsidy to reduce their monthly mortgage payment. Income of borrowers receiving payment subsidy is reviewed at least annually to confirm the borrower's eligibility and adjust the subsidy amount. Please ensure that Mr. and Mrs. Smith receive the proper income receipt documentation (typically IRS Form 1099) of lease proceeds/ royalties so that the Smith's can report this income to Rural Development.

Sincerely,

Area Specialist

cc: Mr. & Mrs. Smith
USDA CSC, Field Assistance Desk, St. Louis, MO.
Housing Division, Harrisburg, PA

SAVED AS: H/W/ SAMPLE RESPOSE TO OIL- GAS LEASING COMPANY-EXISITING LEASE

SAMPLE RESPOSE TO BORROWER-EXISTING OIL / GAS LEASE

DATE

Mr. and Mrs. Robert Smith
100 Main Street
Rural, PA 19999

RE: Notification of Oil & Gas Lease on your USDA financed property
100 Main street
Rural, PA 19999

Dear Mr. and Mrs. Smith:

USDA Rural Development has been contacted by ABC Oil & Gas Corporation and advised that you have executed an oil and gas lease with them on September 20, 2010. In accordance with Rural Development regulations found at 7 CFR 3550.159 (a), borrowers must obtain Agency authorization before leasing mineral rights on their security property. In this case, it does not appear that you contacted the Agency for approval before executing the lease.

Please be advised that income derived from an oil and gas lease must be reported to the USDA Centralized Servicing Center (CSC) and considered when payment assistance for your loan is calculated. If you are receiving or have been receiving income from the aforementioned gas and oil lease that is not or has not been reported to the Agency, please contact CSC Customer Service at 1-800-414-1226 immediately to discuss this situation and your account.

A sample copy of Form RD 3550-23 "Applicant Orientation Guide" that was reviewed with you prior to your loan closing is enclosed for your reference. Please refer to page four (4) for a further explanation on the lease of security property and informing the Agency on changes to the household income.

Sincerely,

Area Specialist

cc: USDA CSC, Field Assistance Desk, St. Louis, MO.
Housing Division, Harrisburg, PA

SAVED AS: H/W/ SAMPLE RESPOSE TO BORROWER-EXISTING OIL- GAS LEASE.DOC

SAMPLE RESPOSE TO BORROWER-PROPOSED OIL / GAS LEASE

DATE

Mr. and Mrs. Kevin Brown
5 Spring Lane Road
Rural, PA 19999

RE: Notification of Oil & Gas Lease on your USDA financed property
5 Spring Lane Road, Rural, PA 19999

Dear Mr. and Mrs. Brown:

Thank you for contacting us with regard to your interest in executing an oil and gas lease with ABC Oil & Gas Corporation. Rural Development regulations found at 7 CFR 3550.159 (a), authorizes the Agency to consent to an oil and gas lease and subordinate our lien to the lessee's rights and interests in their lease if the security property will remain suitable as a residence and the Government's security interest will not be adversely affected.

Furthermore, please be advised that the subordination of the Agency's loan to an oil and gas lease does not entitle you as the leaseholder to proceeds from the lease. Income from the lease will need to be applied to reduce the principal of your loan. However, with acceptable documentation, the Agency can consider paying from lease proceeds customary and reasonable costs related to the transaction. With prior consent of the Agency, this could include the payment of real estate taxes to conclude the lease transaction, title examination, property survey, title insurance, and reasonable attorney and other professional fees.

To make the determination that the proposed lease is acceptable, the Agency requires the following documentation from you. We strongly encourage you to seek legal representation on this matter. Please keep in mind that legal expenses can be considered for reimbursement. However, this would be only in those cases where the Agency consents to the lease transaction.

Please forward the following documentation for our review:

1. Legible copy of the proposed lease.
2. Executed Form RD 465-1 "Application for Partial Release, Subordination, or Consent".
3. Executed Form RD 443-16 "Assignment of Income from Real Estate Security".
4. Detailed explanation of expenses which are being requested to be paid from lease proceeds.

5. Documentation from the oil and gas company that any potential environmental issues will be resolved by the oil and gas company at no cost to the Government or you, the USDA borrower.

6. Please be advised that an appraisal is required for the Agency to subordinate its interest if the amount of the lease proceeds exceeds \$5,000.

A sample copy of Form RD 3550-23 "Applicant Orientation Guide" that was reviewed with you prior to your loan closing is enclosed for your reference. Please refer to item # 6 on page four (4) for a further explanation on the lease of security property.

Sincerely,

Area Specialist

cc: Housing Division, Harrisburg, PA

Enclosed:

Form RD 465-1 "Application for Partial Release, Subordination or Consent".

Form RD 443-16 "Assignment of Income from Real Estate Security".

SAVED AS: H/W/ SAMPLE RESPOSE TO BORROWER-PROPOSED OIL- GAS LEASE.DOC