USDA Rural Development
U.S. DEPARTMENT OF AGRICULTURE

Combination Construction to Permanent Loans

Single Family Housing Guaranteed Loan Program

Welcome to the Combination Construction to Permanent Loans online training module presented by USDA's Single Family Housing Guaranteed Loan Program.

- Does the risk of new construction prevent you from offering this option to potential customers?
- What if you could minimize that risk by obtaining a 90% loan guarantee before construction even begins?
- With Rural Development's Combination Construction to Permanent loans (aka Single-Close loans), approved lenders can help build the dreams of rural Americans while increasing their productivity and profitability with little risk.
- During construction, lenders are protected with a 90% loan guarantee!

Traditional New Construction

New home construction typically consists of two loans.

First Loan: Short term construction loan >>> Usually 12 months

Eligible Rural Area   Buildable Lot   New Construction

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- So how does a traditional new construction, non-single close loan work?
- New home construction typically consists of two separate loans.
- The first is a short term construction loan and the second is a long term “take out” loan for permanent financing, usually a 30 year home loan.
- To begin, the potential new homeowner applies for and closes a short term construction loan, typically for no more than a 12 month term.
- Construction commences and the home construction contractor begins periodic money draws against the construction loan.

Traditional New Construction

Second Loan: Construction complete >>> Apply for 30-year loan

- **Construction is complete**
- **Certificate of occupancy issued**
- **Apply for 30-year home loan**

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- When construction is finished and the certificate of occupancy issued the first loan is complete.
- The construction loan balance must now be rolled in to a new 30 year home loan.
- To accomplish this the home owner begins a new application process for the long term loan.
- As you can see this involves a second loan closing.
- Closing a loan always generates additional fees and expenses.

HB-1-3555, Chapter 12, Section 6
7 CFR Part 3555 Subpart 3555.105

How does a Single Close home loan work?

One set of loan documents bind both the construction and 30-year loan.

1. Construction loan
2. 30-year loan

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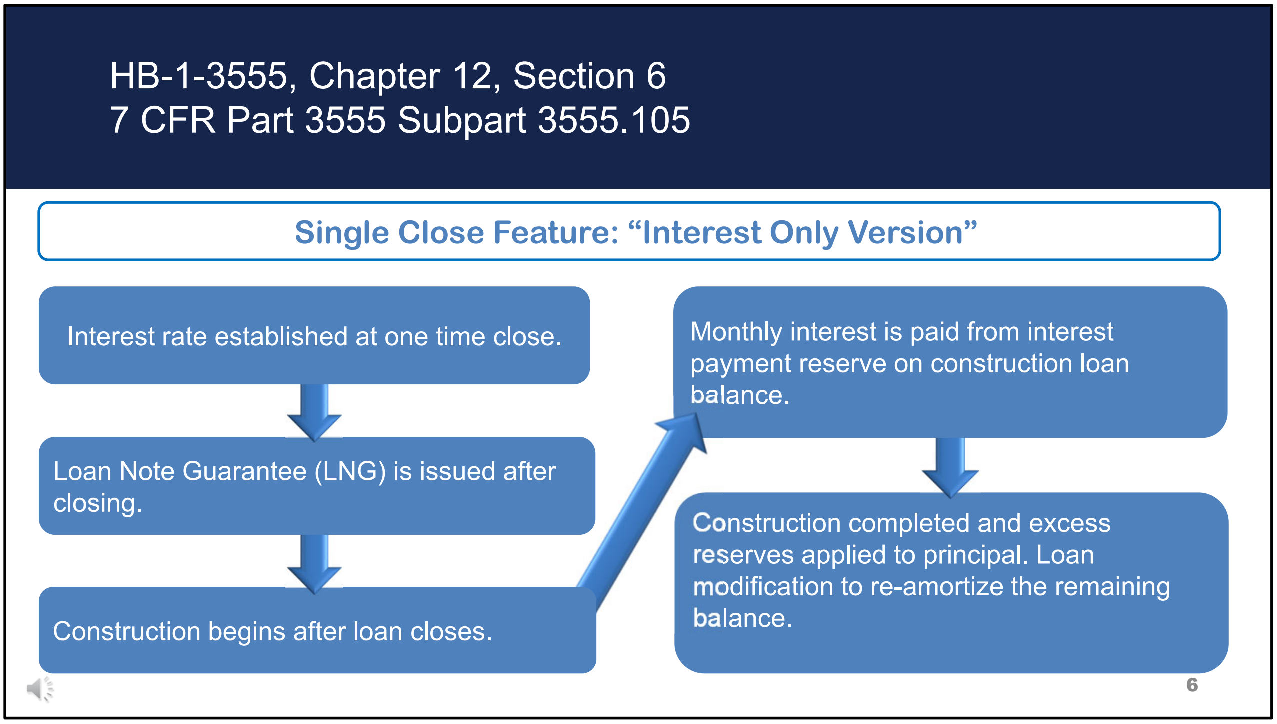
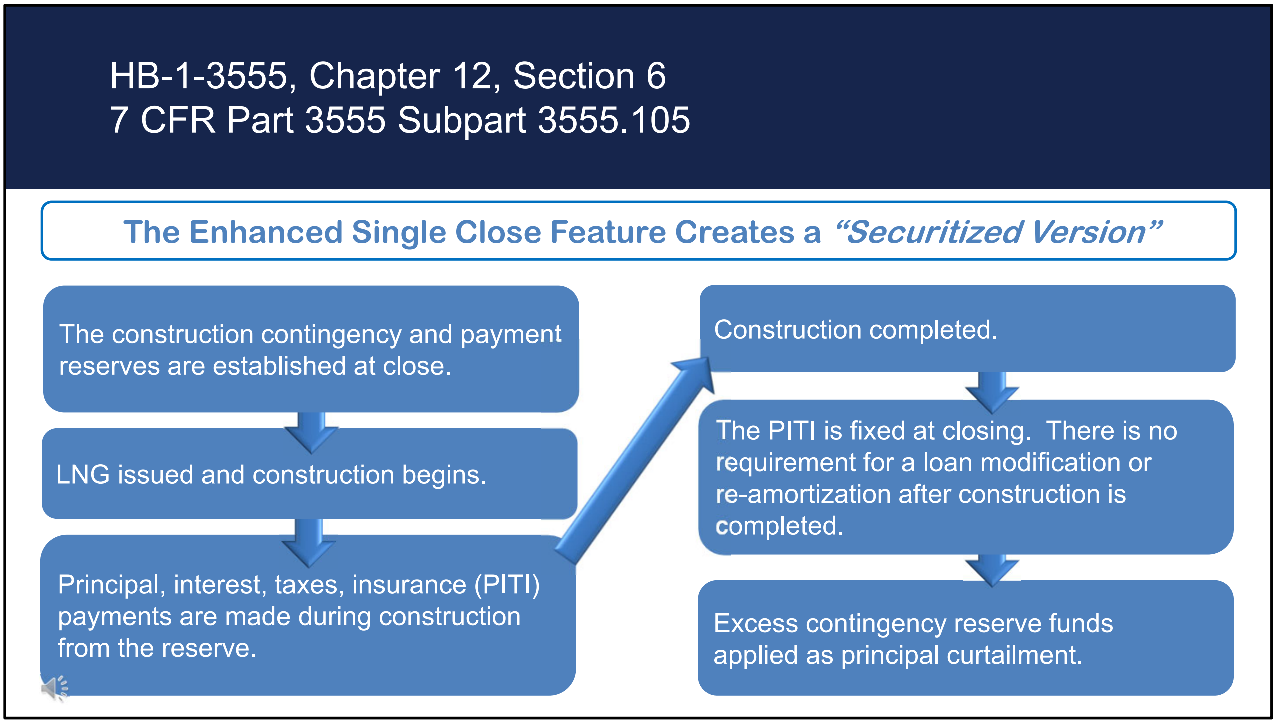
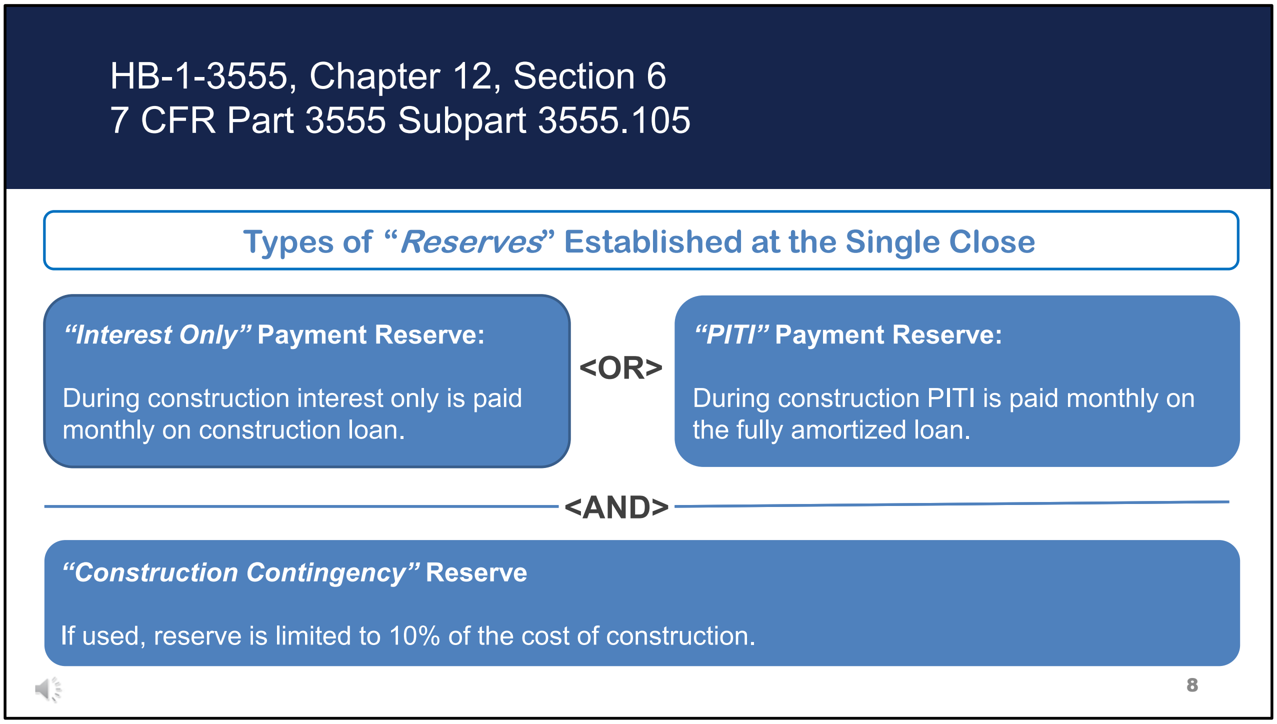
- Now let's introduce the single close loan.
- The single close loan process is utilized to close both the short term construction loan and long term permanent home loan simultaneously.
- The interest rate is fixed for both loans.
- The borrower only needs to sign one set of loan documents binding both the construction and long term loan.
- This process can save closing cost expenses due to the "single close."
- Approved lenders must have appropriate construction lending experience and adequate controls for interim construction cost disbursements



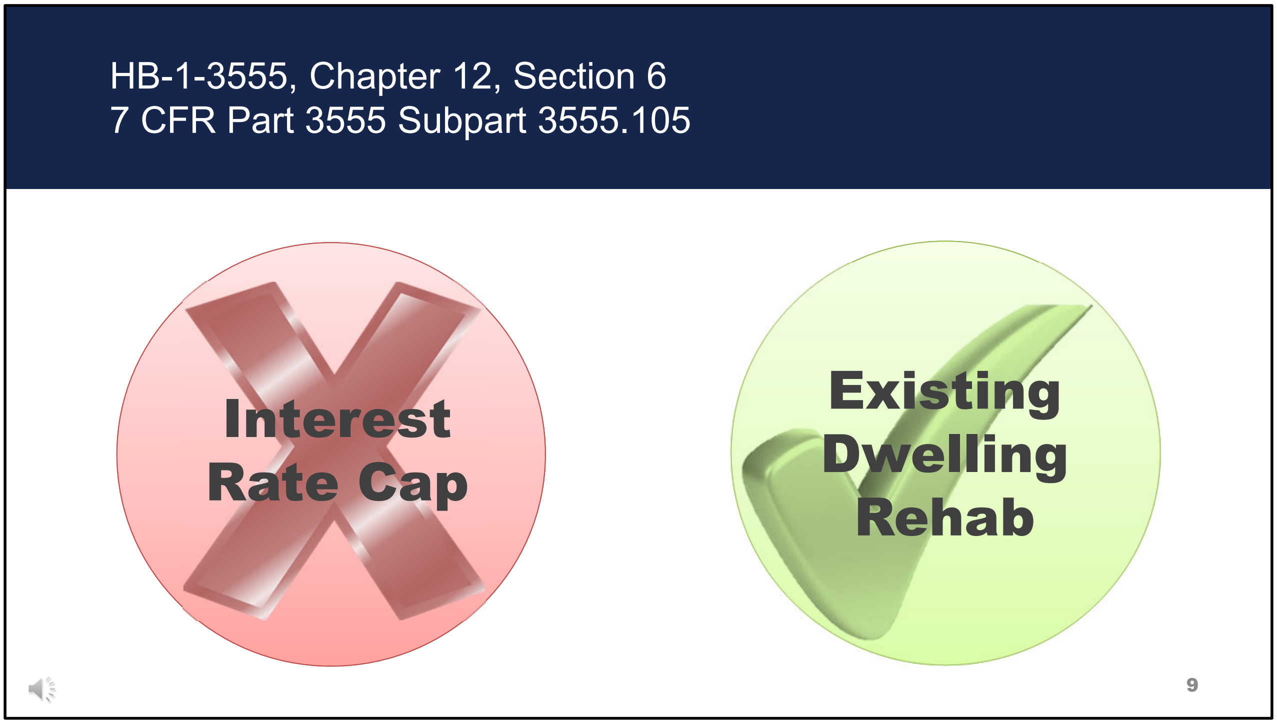
- The single close "interest only" option establishes the permanent interest rate and may also establish up to a 10% construction contingency reserve as well as an interest payment reserve at closing, which happens prior to construction.
- The Loan Note Guarantee is issued after this closing, and the lender is protected before a shovel goes in the ground.
- The lender manages construction loan fund disbursements while loan interest is paid during construction from the established interest reserve.
- When construction is complete excess reserve funds are used as principal curtailment and the loan is then modified (or re-amortized) to achieve full loan term repayment.



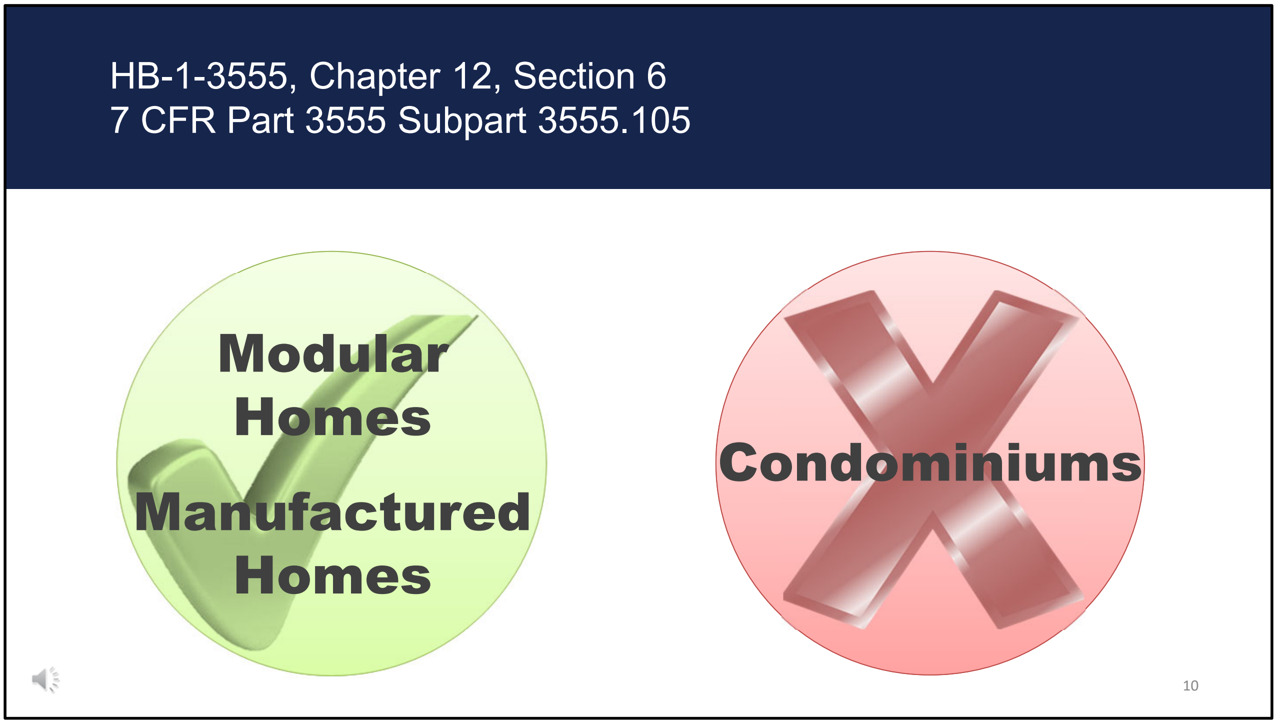
- The second option, the "securitized" version, features the establishment of a principal, interest, taxes and insurance (PITI) reserve at close to make payments during construction.
- The PITI is fixed at close thus eliminating the need for loan modification when construction is complete.
- This permits the loan to be securitized and sold on the secondary financial market, as long as there is no modification or re-amortization after construction is completed.
- When construction is completed any excess reserve funds will be applied as principal curtailment.



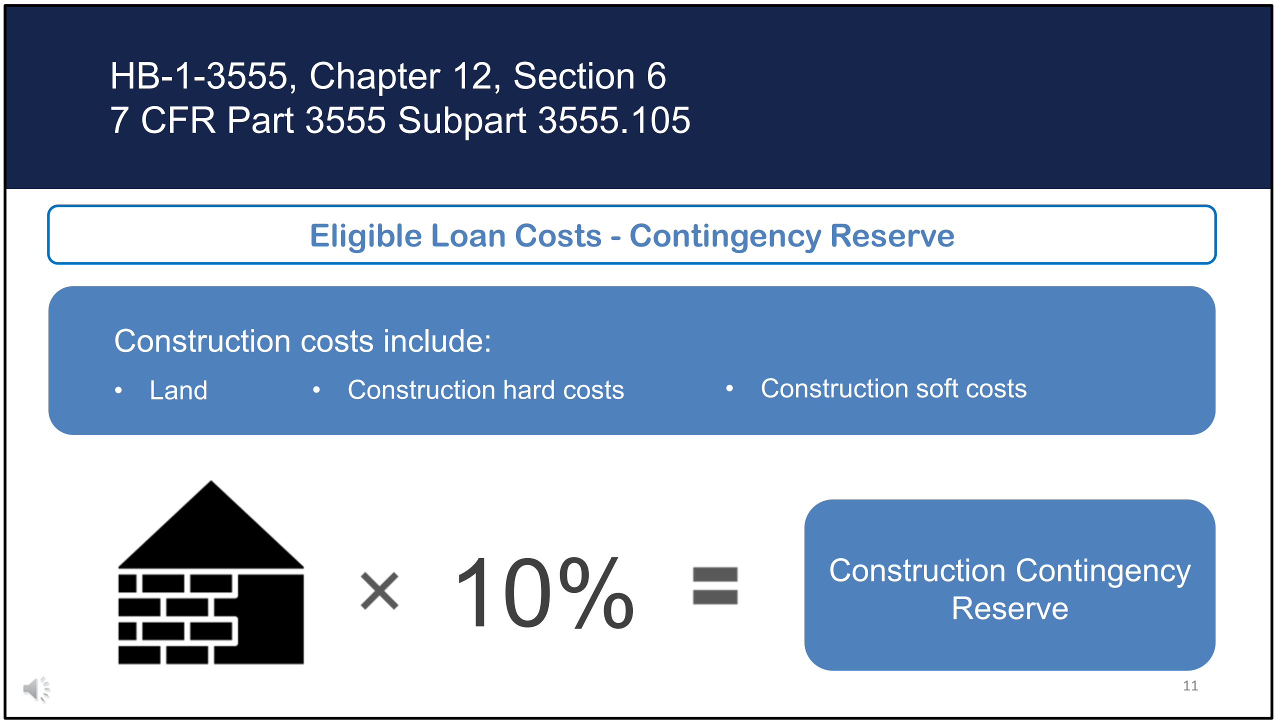
- To recap, there are three types of reserves but only two types may be used with any single close loan.
- Either the interest only or PITI payment reserve will be established at loan close.
- Then if used, the construction contingency reserve of up to 10% of construction costs will also be established at loan close.
- When construction is complete, excess funds from payment and construction reserves will be applied as principal curtailment.



- Please note that the July 22, 2019 Final Rule, which became effective October 1, 2019, eliminates the interest rate cap for all loans.
- In addition, it provided for rehabilitation and repair loans with the purchase of an existing dwelling.



- Now for eligible loan costs.
- The single close loan will be used to finance the construction of a new single-family housing residence, which can include modular and manufactured home construction.
- Condominiums, including detached condominiums and site condominiums, are ineligible for this type of loan feature.



- Any item included in the cost to construct the home must be commonly and customarily included in the cost to construct other homes in the area where the subject property is located.
- A construction contingency reserve to cover eligible expenses associated with unplanned problems with construction or change orders may be utilized.
- If used, the reserve can be up to 10% of the cost of construction which includes labor, materials and soft costs.
- It is not required that the reserve be 10% if it is not necessary for the build; there does not have to be any contingency reserve.
- Unused contingency reserve funds after construction are applied as a principal reduction.
- Make sure you review all details of eligible loan costs in handbook section 12.15.

HB-1-3555, Chapter 12, Section 6
7 CFR Part 3555 Subpart 3555.105

Eligible Loan Costs - Payment Reserve

Loan term = 30 years

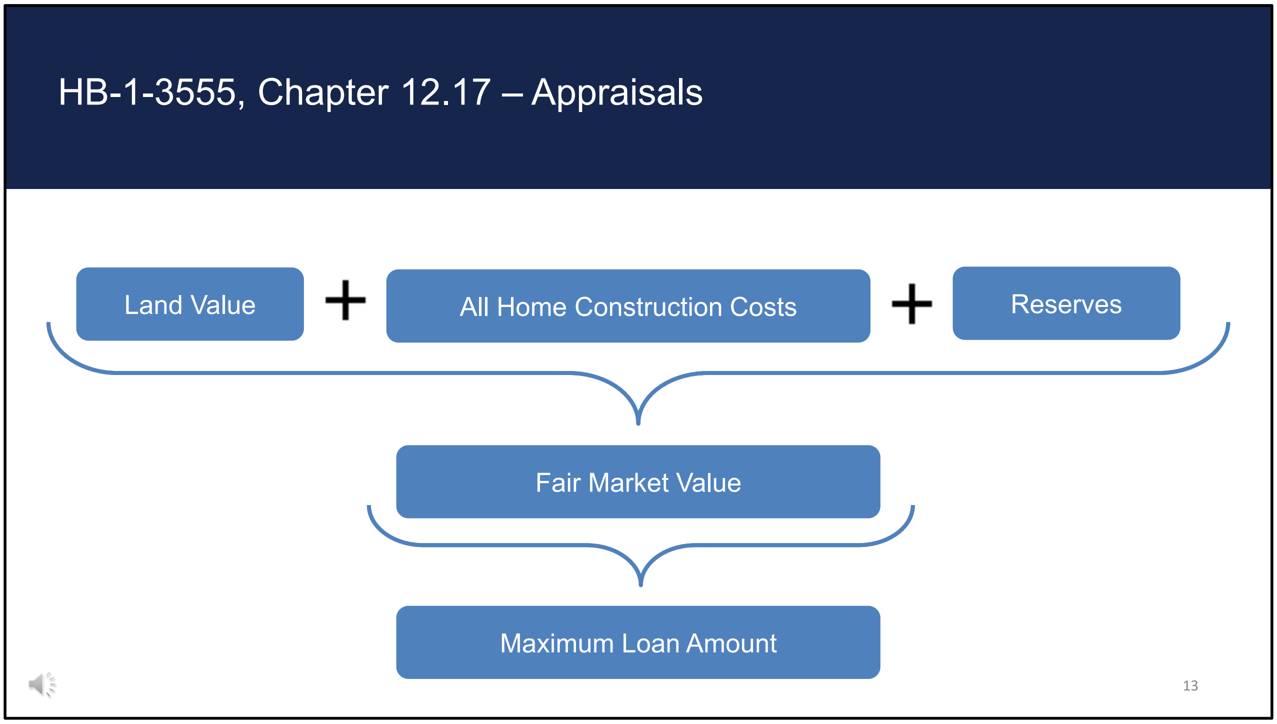
Fixed interest rate

Payment reserve account can be:
“Interest Only” <or> “PITI Reserve”

If no PITI reserve, then an interest only reserve can be established from loan funds at closing to cover the construction loan payments during construction.

At construction completion any excess funds from the payment reserve account will be applied as principal curtailment.

- At closing, the term of the loan is for thirty years.
- During construction, either the PITI payments or the interest-only payments are payable monthly either directly from the borrower or drawn from the payment reserve account.
- As with the contingency reserve, as discussed in the prior slide, any left-over payment reserve funds must be applied as a principal reduction.



- Appraisals are an important part of the loan process by establishing the maximum loan amount.
- The fair market value is determined by a licensed or certified appraiser in accordance with regulation 7 CFR 3555.107(d).
- The proposed (to-be constructed) subject property will be utilized to establish the maximum loan amount.
- Land value is based on the value as reported in the Appraisal Report, with no seasoning requirement.
- It is crucial that the appraiser has all information regarding costs, including all soft costs, hard costs, and the necessary payment and contingency reserves, at the beginning of the appraisal process.
- Incomplete appraiser data will result in a flawed maximum loan to value calculation and incorrect borrower financing amounts.
- Handbook Chapter 12, Section 2: APPRAISALS details appraisal requirements.

LEARNING CHECKS

7 CFR Part 3555 / HB-1-3555

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The best way to learn information is to test your knowledge!

QUESTION

Topic

- Question will be bulleted with scenario, or
- Include a statement/question

TRUE/FALSE or other answer options will be displayed

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The following question slides will list:

- The topic,
- A question or scenario, and
- potential responses.

ANSWER

Topic

7 CFR Part 3555 and HB-1-3555 references provided

X. Correct Response

- Additional guidance for clarification may be provided

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The answer slides will list:

- The topic,
- the reference to the answer from the regulation and handbook,
- the correct response, and
- any additional clarification that may be helpful.

Ready?

LET’S GET STARTED!

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Let’s get started!

QUESTION

Combination Construction to Permanent Loans

Approved lender responsibilities are to:

A. Monitor construction of the subject property.
B. Oversee disbursement of mortgage proceeds.
C. Obtain documentation that confirms the construction of the subject property is complete.
D. All of the above.

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.13 – Lender Requirements

D. All of the Above

Approved lenders will be responsible for monitoring construction of the subject property, overseeing disbursement of mortgage proceeds, and obtaining documentation that confirms the construction of the subject property is complete.

- The answer is D.
- Approved lenders will be responsible for monitoring construction of the subject property, overseeing disbursement of mortgage proceeds, and obtaining documentation that confirms the construction of the subject property is complete.

QUESTION

Combination Construction to Permanent Loans

USDA will certify that the lender is utilizing a fixed price construction contract **and** that the lender has staff with two or more years experience in construction making and administering construction loans.

A. TRUE B. FALSE

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.13 – Lender Requirements

B. FALSE

- **Lenders will ensure** the utilization of a fixed price construction contract.
- Lenders will: Provide a fully executed Form RD 3555-16 lender agreement and **self-certify** that they have staff with two or more years' experience making and administering construction loans.

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USDA does not certify lenders' credentials. Lenders will self certify that they have staff with two or more years' experience making and administering construction loans. The lender will also ensure the utilization of a fixed price construction contract.

QUESTION

Combination Construction to Permanent Loans

It is the lender's sole responsibility to disburse mortgage proceeds whenever the builder calls for funds to pay construction expenses.

A. TRUE B. FALSE

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.13 – Lender Requirements

B. FALSE

Lenders will: Approve and disburse mortgage proceeds in accordance with the construction loan agreement, **with prior written approval by the borrower** and confirmation of work completion prior to disbursement.

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The answer is false as the lender will approve and disburse mortgage proceeds in accordance with the construction loan agreement, with **prior written approval by the borrower** and confirmation of work completion prior to disbursement.

QUESTION

Combination Construction to Permanent Loans

The approved lender, not USDA will be responsible for approving participating builders.

A. TRUE   B. FALSE

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.14 – Construction Contractor-Builder Requirements

A. TRUE

The approved lender and their agent, if any, will be responsible for approving participating builders.

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The answer is true as the approved lender and their agent, if any, will be responsible for approving participating builders.

QUESTION

Combination Construction to Permanent Loans

The single close loan can be used to finance the construction of a new single-family housing residence, which can include:

A. Modular home
B. Manufactured home
C. Condominiums, including detached and site condominiums
D. All of the above

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.15 – Eligible Loan Costs

A. and B.

The loan will be used to finance the construction of a new single-family housing residence, which can include **modular** and **manufactured** home construction. **Condominiums**, including detached condominiums and site condominiums, **are ineligible** for this type of loan feature.

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Eligible loan costs for the construction of a new single-family home can include modular and manufactured home but excludes condominiums, including detached condominiums and site condominiums,

QUESTION

Combination Construction to Permanent Loans

- Eligible loan costs are land, construction hard costs, and construction soft costs.
- Ineligible loan costs are the interest only reserve and PITI reserve.

A. TRUE   B. FALSE

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.15 – Eligible Loan Costs

B. FALSE

Loan costs which may be included in the loan amount are subject to the maximum loan to value and will be reasonable and customary construction costs such as:

- **Construction contingency** reserve
- **Interest reserve** including interim interest as accrued, during the construction period, on a warehouse line of credit up to 12 months
- Principal, interest, taxes, and insurance **(PITI) payment reserve** up to 12 months

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The answer is false as the construction contingency reserve and either the interest reserve or PITI reserve is an eligible loan cost.

QUESTION

Combination Construction to Permanent Loans

What items does the appraiser include to determine subject property fair market value? Choose all that apply.

A. Acquisition cost of land
B. Construction hard costs inside of contract
C. Construction hard costs paid to subcontractors outside of contract
D. Furniture & major electronics
E. Appraisal fees
F. Architecture fees
G. Title fees
H. Construction contingency reserve
I. Interest payment reserve
J. PITI payment reserve
K. Builder acceptance or review fees

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.15 – Eligible Loan Costs

All Except D

- The only item the **appraiser will not use** to establish fair market value is:

  "D. Furniture and major electronics"
- All other items are eligible loan costs and will be included in appraisers fair market value calculation.
- Make sure you review 12.15 Eligible Loan Costs, Land, Construction Hard Costs and Construction Soft Costs to understand all that is included in appraiser's fair market value calculation.

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- All listed items except "D. Furniture and major electronics"
- All other items are eligible loan costs and will be included in appraisers fair market value calculation.
- Make sure you review 12.15 Eligible Loan Costs, Land, Construction Hard Costs and Construction Soft Costs to understand all that is included in appraiser's fair market value calculation.

QUESTION

Combination Construction to Permanent Loans

The lender is responsible for approving disbursements to the builder.

A. TRUE B. FALSE

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Read the question on the slide and select a response.

ANSWER

Combination Construction to Permanent Loans

HB 12.23 – Construction Draws

B. FALSE

The **borrower and lender** will be jointly responsible for approving disbursements to the builder during the construction phase.

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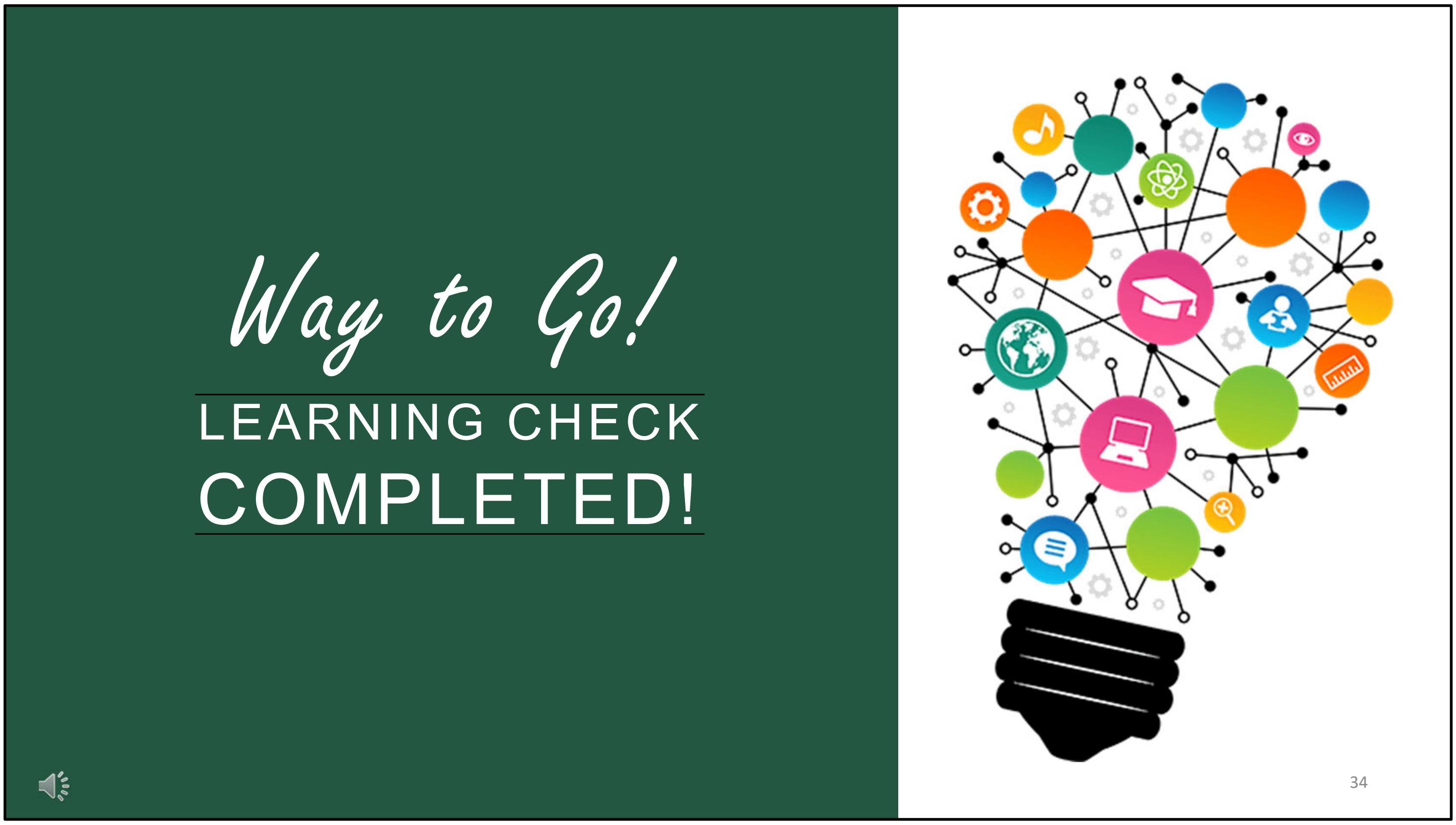
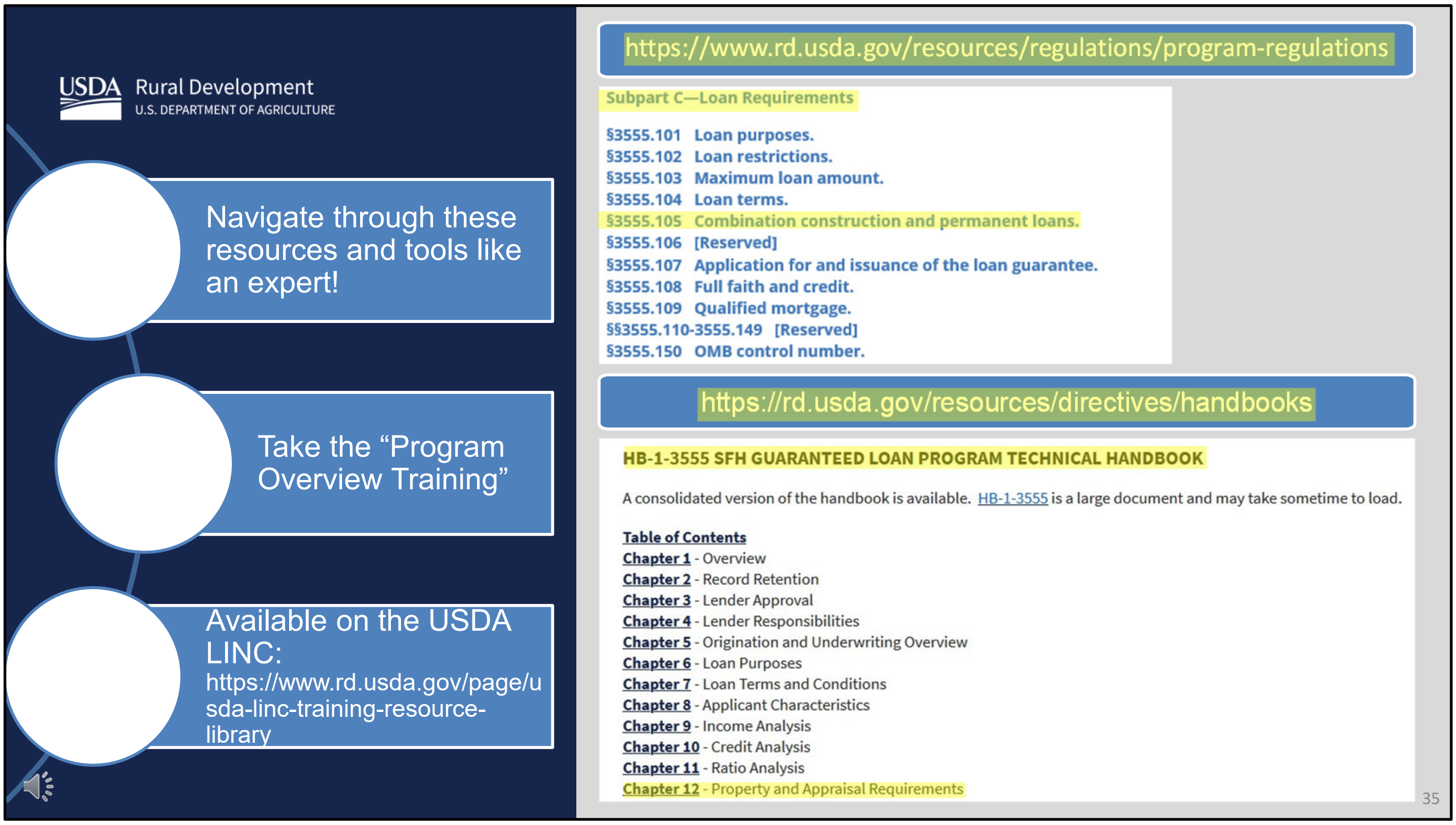
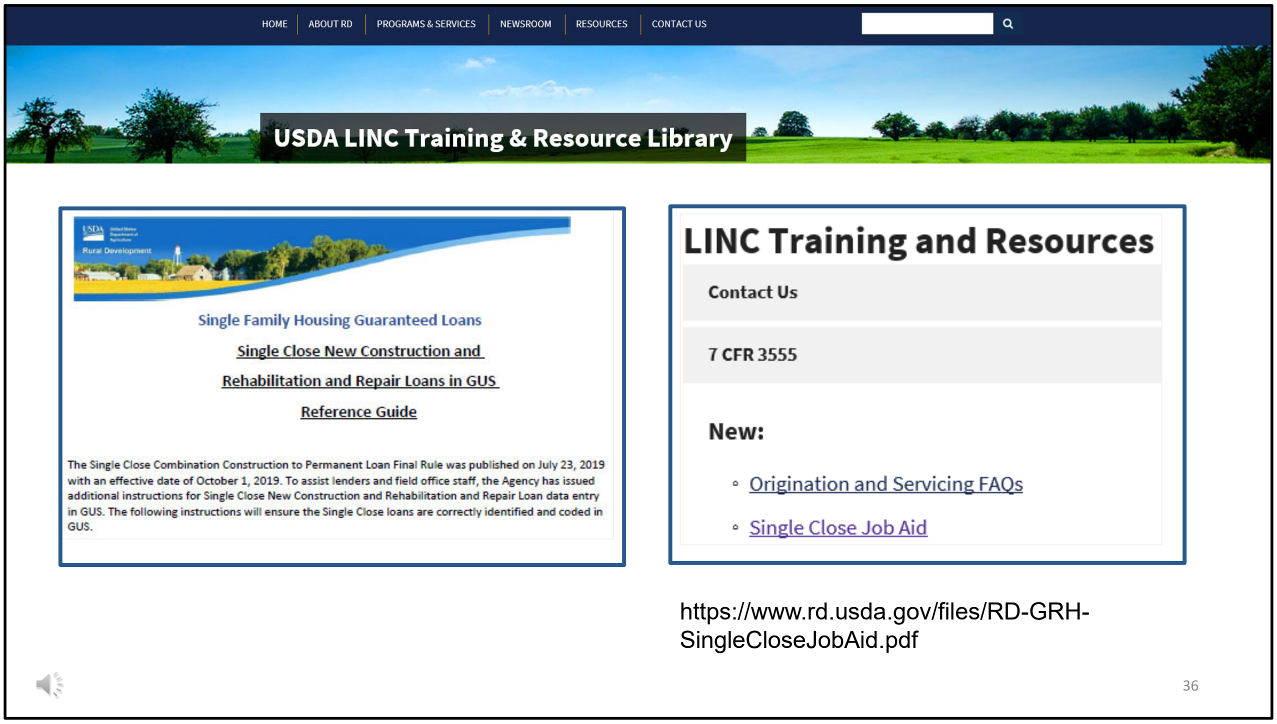
The answer is false as the **borrower and lender will be jointly responsible** for approving disbursements to the builder during the construction phase



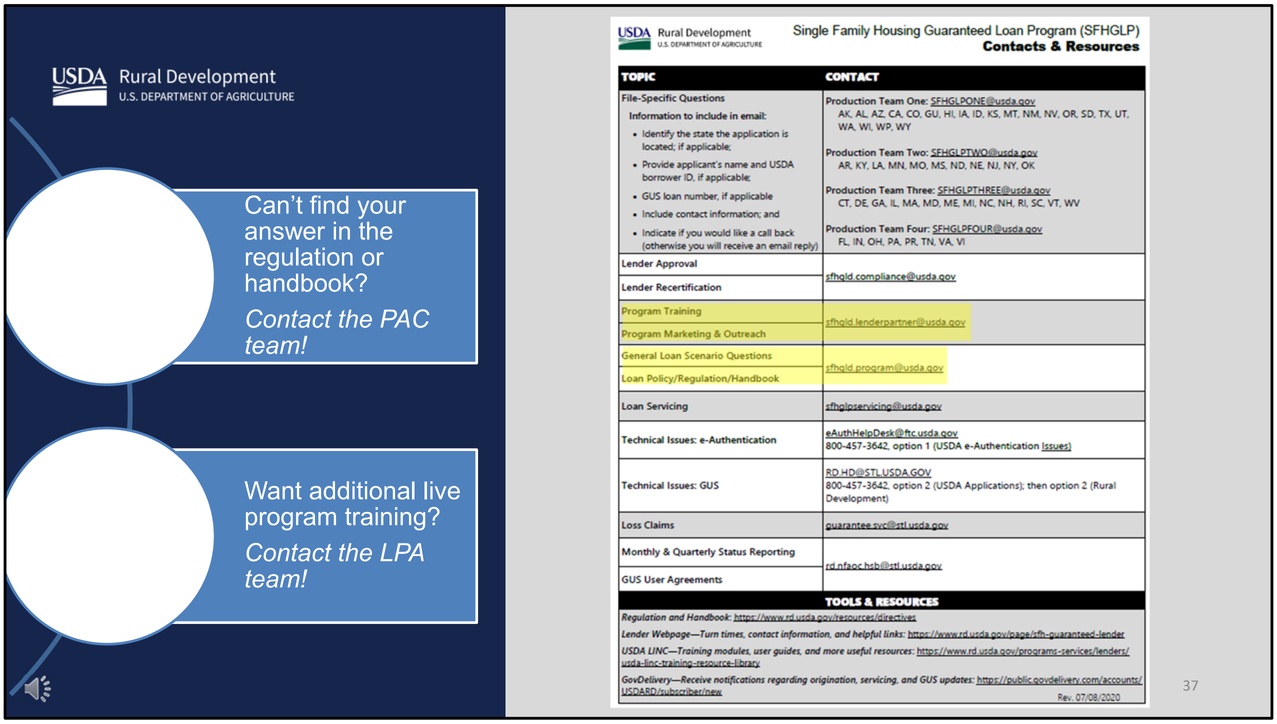
Way to go! You have completed the learning checks!



- This training module has provided you with an overview of the key requirements of a Combination Construction to Permanent loan.
- Complete program requirements and guidance can be found in 7 CFR Part 3555, Subpart C, Section 3555.105 and Chapter 12 of HB-1-3555 in section 6.
- Be sure to bookmark these references, save yourself valuable time by using Cntrl-F to quickly search and find answers, and always ensure you are referencing the most current publications.
- The "Program Overview Training" module will assist you in learning how to navigate through all the resources and tools Rural Development has created to assist you.



- In addition to the other resources and tools available to assist lenders, the agency has developed a Single Close Job Aid to be used specifically for construction to permanent loans.
- The Single Close Job Aid, available at the USDA LINC Training & Resource Library, provides step by step instructions on how to properly identify and input single close applications in GUS.



- Users should first look for answers to their questions in the regulation and handbook, but if you still have a question after reviewing your resources, we're here to help.
- All policy and regulation questions regarding the topic we just covered should be sent to our Policy, Analysis, and Communications Branch and
- If you would like to request additional program training, contact our Lender and Partner Activities Branch.

Thank you for supporting the USDA Single Family Housing Guaranteed Loan Program and America's rural homebuyers!

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EQUAL HOUSING OPPORTUNITY

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This will conclude the training module. Thank you and have a great day!