

**DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT**
24 CFR Parts 200 and 203
[Docket No. FR-4592-F-02]
RIN 2502-AH51
**Single Family Mortgage Insurance;
Section 203(k) Consultant Placement
and Removal Procedures**

AGENCY: Office of the Assistant Secretary for Housing-Federal Housing Commissioner, HUD.

ACTION: Final rule.

SUMMARY: This final rule establishes placement and removal procedures for HUD's list of qualified consultants under the Section 203(k) Rehabilitation Loan Insurance Program. A 203(k) lender may select a qualified independent consultant, who is an expert in the field of home inspection, cost estimating, and construction, to perform various tasks required for the rehabilitation of the property. The establishment of these placement and removal procedures will better protect 203(k) borrowers and lenders, and safeguard Federal Housing Administration (FHA) insurance funds. This final rule follows publication of an October 24, 2001 proposed rule.

DATES: *Effective Date:* September 9, 2002.

Comment Due Date: October 8, 2002.

ADDRESSES: Interested persons are invited to submit comments regarding this rule to the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410. Communications should refer to the above docket number and title. Facsimile (FAX) comments are not acceptable. A copy of each communication will be available for public inspection and copying between 7:30 a.m. and 5:30 p.m. weekdays at the above address.

FOR FURTHER INFORMATION CONTACT: Vance T. Morris, Director, Office of Single Family Program Development, Room 9266, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410-8000; telephone (202) 708-2121 (this is not a toll-free number). Hearing- or speech-impaired individuals may access this number via TTY by calling the toll-free Federal Information Relay Service at (800) 877-8339.

SUPPLEMENTARY INFORMATION
**I. Background—The October 24, 2001
Proposed Rule**

On October 24, 2001 (66 FR 53930), HUD published a proposed rule for public comment to establish placement and removal procedures for HUD's list of qualified consultants under the Section 203(k) Rehabilitation Loan Insurance Program. The 203(k) Program is the primary Federal Housing Administration (FHA) program for the rehabilitation and repair of single family properties. Section 203(k) loan insurance enables homebuyers and homeowners to finance both the purchase (or refinance) of a house and the cost of its rehabilitation through a single mortgage.

One of the most time consuming and difficult parts of the 203(k) loan process is for the borrower to properly prepare the required cost estimate, work write-up, and architectural exhibits. A borrower using the 203(k) Program may choose to have a qualified independent consultant, who is an expert in the field of home inspection, cost estimating, and construction, perform these tasks. The lender will then select a consultant and determine the scope of the work to be performed. The use of a consultant by the borrower is not required. However, many borrowers choose to use consultants to expedite processing of their 203(k) loans.

HUD, through its four Homeownership Centers (HOCs), maintains lists of qualified consultants on the applicable internet website. A lender may only select a consultant included on a HOC's list. Presently, there are no regulatory procedures for placing a consultant on, nor for removing a poorly performing consultant from the list. HUD published the October 24, 2001 proposed rule to establish such policies and procedures. The establishment of these placement and removal procedures will better protect 203(k) borrowers and lenders, and safeguard the FHA insurance fund. The October 24, 2001 proposed rule provides additional details regarding the 203(k) consultant placement and removal procedures.

II. This Final Rule

This final rule follows publication of the October 24, 2001 proposed rule. The public comment period on the proposed rule closed on December 24, 2001. HUD did not receive any public comments on the proposed rule; however, it has made three changes to the policies and procedures contained in the October 24, 2001 proposed rule.

First, the final rule no longer provides that a 203(k) consultant may be removed from HUD's list for having served as the consultant on properties in foreclosure, default, or claim status. HUD has determined that further consideration is required regarding this provision of the proposed rule, and the preamble of this rule, in Section IV, requests comment on specific issues related to establishing such a provision. After considering any comments that are received, should HUD at a future date decide to provide for the removal of 203(k) consultants based on excessive claim and default rates, it will do so through issuance of a new proposed rule.

Secondly, this final rule clarifies that a consultant may be removed from the 203(k) Consultant Roster for failure to retain standing as a state licensed home inspector, if the consultant is located in a state that requires such licensing. This final rule (as did the preceding October 24, 2001 proposed rule) provides that such licensing is required for placement on the Roster, but the proposed rule failed to specify that failure to maintain the licensing constituted grounds for removal. The final rule provides the necessary clarification.

Finally, § 203.50(l) of this final rule clarifies that, once a 203(k) borrower chooses to use the services of a consultant, the lender must select a consultant that has been placed on the 203(k) Consultant Roster. The proposed regulatory language would only have provided that a lender "may" select a consultant placed on the Roster. This language might have caused some 203(k) lenders to incorrectly assume that consultants not included on the Roster were eligible for selection.

**III. Small Business Concerns Related to
the Removal of Consultants**

With respect to removing a 203(k) consultant from the list, or taking other appropriate enforcement action against a consultant, HUD is cognizant that section 222 of the Small Business Regulatory Enforcement Fairness Act of 1996 (Public Law 104-121) (referred to as "SBREFA") requires the Small Business and Agriculture Regulatory Enforcement Ombudsman to "work with each agency with regulatory authority over small businesses to ensure that small business concerns that receive or are subject to an audit, on-site inspection, compliance assistance effort or other enforcement related communication or contact by agency personnel are provided with a means to comment on the enforcement activity conducted by this personnel." To implement this statutory provision, the Small Business Administration has

requested that agencies include the following language on agency publications and notices that are provided to small businesses concerns at the time the enforcement action is undertaken. The language is as follows:

Your Comments Are Important

The Small Business and Agriculture Regulatory Enforcement Ombudsman and 10 Regional Fairness Boards were established to receive comments from small businesses about federal agency enforcement actions. The Ombudsman will annually evaluate the enforcement activities and rate each agency's responsiveness to small business. If you wish to comment on the enforcement actions of [insert agency name], call 1-888-REG-FAIR (1-888-734-3247).

As HUD stated in its notice describing HUD's actions on the implementation of SBREFA, which was published on May 21, 1998 (63 FR 28214), HUD intends to work with the Small Business Administration to provide small entities with information on the Fairness Boards and National Ombudsman program, at the time enforcement actions are taken, to ensure that small entities have the full means to comment on the enforcement activity conducted by HUD.

IV. Request for Public Comment

HUD seeks to establish clear, consistent and familiar standards and procedures for a consultant to maintain status on, or be removed from, the 203(k) Consultant Roster. HUD is therefore seeking comment on whether, and if so, in what manner, it should establish "serving, or having served, as the rehabilitation consultant for properties securing 203(k) mortgages of which a significant percentage are in foreclosure, default or claim status" as a basis for removal from the Roster. In particular, HUD requests comments on the following issues:

1. Whether HUD should establish a minimum number of consultations as a threshold for any action, and if so, what number would be appropriate.
2. Whether HUD should specify the age of 203(k) mortgages that would be considered under a standard, and what age would be appropriate (e.g., consultations on properties securing 203(k) mortgages not more than one, two or three years old).
3. What percentage of foreclosure, default or claims should be considered.
4. What period of time over which consultations are conducted should be used for evaluation purposes (e.g., consultations over 12 months, or 18 months, or 24 months)?
5. What factors in addition to the percent of loan defaults, foreclosures

and claims should HUD consider in evaluating consultant performance?

6. Should the severity of loss be considered as a factor in evaluating a consultant's performance?

7. If included as a factor, how should severity of loss be considered in evaluating performance?

8. What kinds of factors should be considered as mitigating for a consultant with higher than normal default, foreclosure and claim rates?

9. What are appropriate procedures and factors to consider for removal?

10. What is an appropriate period of removal from the Roster before a reinstatement is permitted?

11. What are appropriate procedures and factors to consider for reinstatement?

V. Findings and Certifications

Public Reporting Burden

The information collection requirements contained in this final rule have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB Control Number 2502-0527. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

Regulatory Planning and Review

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866, *Regulatory Planning and Review*. OMB determined that this rule is a "significant regulatory action" as defined in section 3(f) of the Order (although not an economically significant regulatory action under the Order). Any changes made to this rule as a result of that review are identified in the docket file, which is available for public inspection in the office of the Department's Rules Docket Clerk, Room 10276, 451 Seventh Street, SW., Washington, DC 20410-0500.

Environmental Impact

This final rule establishes placement and removal procedures for HUD's list of qualified 203(k) rehabilitation loan consultants. The final rule does not direct, provide for assistance or loan and mortgage insurance for, or otherwise govern or regulate, real property acquisition, disposition, leasing, rehabilitation, alteration, demolition, or new construction, or establish, revise, or provide for standards for construction or construction materials, manufactured

housing, or occupancy. Accordingly, under 24 CFR 50.19(c)(1), this final rule is categorically excluded from environmental review under the National Environmental Policy Act (42 U.S.C. 4321 *et seq.*).

Regulatory Flexibility Act

The Secretary has reviewed this final rule before publication, and by approving it certifies, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), that this final rule will not have a significant economic impact on a substantial number of small entities. The reasons for HUD's determination are as follows.

The final rule establishes the procedure by which a consultant, who has violated FHA single family mortgage insurance program requirements, may be removed from HUD's list of qualified 203(k) consultants. Accordingly, to the extent that this final rule impacts small entities it will be as a result of actions taken by small entities themselves—that is, violation of single family program regulations and requirements.

Further, the final rule provides several procedural safeguards designed to minimize any potential impact on small entities. For example, the rule grants consultants, selected for removal from the list, the opportunity to provide a written response and to request a conference regarding a proposed removal. The rule also specifies that the official designated by HUD to review an appeal may not be the same HUD official involved in the initial removal decision. In addition, the examination requirements will be "phased-in" for consultants on the list, and will not take effect until six months after the effective date of promulgation. This delayed effective date will provide consultants on the list with additional time to meet the new requirements.

Executive Order 13132, Federalism

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial direct compliance costs on State and local governments and is not required by statute, or the rule preempts State law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This final rule will not have federalism implications and will not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the Executive Order.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments, and on the private sector. This final rule will not impose any Federal mandates on any State, local, or tribal governments, or on the private sector, within the meaning of the Unfunded Mandates Reform Act of 1995.

Catalog of Federal Domestic Assistance Numbers

The Catalog of Federal Domestic Assistance Number for the Section 203(k) Rehabilitation Loan Insurance program is 14.108.

List of Subjects

24 CFR Part 200

Administrative practice and procedure, Claims, Equal employment opportunity, Fair housing, Home improvement, Housing standards, Incorporation by reference, Lead poisoning, Loan programs—housing and community development, Minimum property standards, Mortgage insurance, Organization and functions (Government agencies), Penalties, Reporting and recordkeeping requirements, Social security, Unemployment compensation, Wages.

24 CFR Part 203

Hawaiian Natives, Home improvement, Indians—lands, Loan programs—housing and community development, Mortgage insurance, Reporting and recordkeeping requirements, Solar energy.

Accordingly, for the reasons described in the preamble, HUD amends 24 CFR parts 200 and 203 as follows:

PART 200—INTRODUCTION TO FHA PROGRAMS

1. The authority citation for 24 CFR part 200 is revised to read as follows:

Authority: 12 U.S.C. 1702–1715z–21; 42 U.S.C. 3535(d).

2. In subpart F, add §§ 200.190–200.193, under a new undesignated center heading reading “Section 203(k) Rehabilitation Loan Consultants,” to read as follows:

Subpart F—Placement and Removal Procedures for Participation in FHA Programs

Section 203(k) Rehabilitation Loan Consultants

§ 200.190 HUD list of qualified 203(k) consultants.

(a) *Qualified consultant list.* HUD maintains a list of qualified consultants for use in the rehabilitation loan insurance program authorized by section 203(k) of the National Housing Act (12 U.S.C. 1709(k)) (referred to as the “203(k) Program”).

(b) *Consultant functions.* Only a consultant included on the list may be selected by the lender to conduct any consultant function under the 203(k) Program (see § 203.50(l) of this title).

(c) *Disclaimer.* The inclusion of a consultant on the list means only that the consultant has met the qualifications and conditions prescribed by the Secretary for placement on the list of consultants qualified for the 203(k) Program. The inclusion of a consultant on the list does not create or imply a warranty or endorsement by HUD of the consultant, nor does it represent a warranty of any work performed by the consultant.

§ 200.191 Placement of 203(k) consultant.

(a) *Application.* To be considered for placement on the list, a consultant must apply to HUD using an application (or materials) in a form prescribed by HUD.

(b) *Eligibility.* To be eligible for placement on the list:

(1) The consultant must demonstrate to HUD that it either:

(i) Has at least three years’ experience as a remodeling contractor, general contractor or home inspector; or

(ii) Is a state-licensed architect or state-licensed engineer;

(2) If located in a state that requires the licensing of home inspectors, the consultant must submit proof of such licensing;

(3) The consultant must submit a narrative description of the consultant’s ability to perform home inspections, prepare architectural drawings, use proper methods of cost estimating and complete draw inspections.

(4) The consultant must certify that it has read and fully understands the requirements of the HUD handbook on the 203(k) Program (4240.4) and all HUD Mortgagee Letters and other instructions relating to the 203(k) Program.

(5) The consultant must not be listed on:

(i) The General Services Administration’s Suspension and Debarment List;

(ii) HUD’s Limited Denial of Participation List; or

(iii) HUD’s Credit Alert Interactive Voice Response System.

(6) The consultant must have passed a comprehensive examination on the

203(k) Program, if HUD has developed such an exam.

(c) *Delayed effective date of examination requirement for consultants currently on the list.*

Consultants who are included on the list on the date when the requirement for the examination described in paragraph (b)(6) of this section becomes effective have until 6 months following this date to pass the comprehensive exam. Failure to pass the examination by the deadline date constitutes cause for removal under § 200.192.

§ 200.192 Removal of 203(k) consultant.

(a) *Cause for removal.* HUD may remove a consultant from the list for any cause that HUD determines to be detrimental to HUD or its programs. Cause for removal includes, but is not limited to:

(1) Poor performance on a HUD quality control field review;

(2) Failure to comply with applicable regulations or other written instructions or standards issued by HUD;

(3) Failure to comply with applicable Civil Rights requirements;

(4) Being debarred or suspended, or subject to a limited denial of participation;

(5) Misrepresentation or fraudulent statements;

(6) Failure to retain standing as a state licensed architect or state-licensed engineer (unless the consultant can demonstrate the required three years experience as a home inspector or remodeling contractor);

(7) Failure to retain standing as a state licensed home inspector, if the consultant is located in a state that requires such licensing; or

(8) Failure to respond within a reasonable time to HUD inquiries or requests for documentation.

(b) *Procedure for removal.* A consultant that is debarred or suspended, or subject to a limited denial of participation will be *automatically* removed from the list. In all other cases, the following procedure for removal will be followed:

(1) HUD will give the consultant written notice of the proposed removal. The notice will state the reasons for, and the duration of, the proposed removal.

(2) The consultant will have 20 days from the date of the notice (or longer, if provided in the notice) to submit a written response appealing the proposed removal and to request a conference. A request for a conference must be in writing and must be submitted along with the written response.

(3) A HUD official will review the appeal and send a response either

affirming, modifying, or canceling the removal. The HUD official will not be someone who was involved in HUD's initial removal decision. HUD will respond with a decision within 30 days of receiving the appeal or, if the consultant has requested a conference, within 30 days after the completion of the conference. HUD may extend the 30-day period by providing written notice to the consultant.

(4) If the consultant does not submit a timely written response, the removal will be effective 20 days after the date of HUD's initial removal notice (or after a longer period provided in the notice). If a written response is submitted, and the removal decision is affirmed or modified, the removal will be effective on the date of HUD's notice affirming or modifying the initial removal decision.

(c) *Placement on the list after removal.* A consultant that has been removed from the list may apply for placement on the list (in accordance with § 200.191) after the period of the consultant's removal from the list has expired. An application will be rejected if the period for the consultant's removal from the list has not expired.

(d) *Other action.* Nothing in this section prohibits HUD from taking such other action against a consultant, as provided in 24 CFR part 24, or from seeking any other remedy against a consultant available to HUD by statute or otherwise.

§ 200.193 Responsibilities of 203(k) consultants on the list.

All consultants included on the list are responsible for:

(a) Obtaining and reading the HUD handbook on the 203(k) Program (4240.4) and any updates to the handbook.

(b) Complying with the HUD handbook on the 203(k) Program (4240.4), and any updates to the handbook, when performing any consultant function under the 203(k) Program.

(c) Obtaining and reading all Mortgagee Letters and other instructions issued by HUD relating to the 203(k) Program.

(d) Complying with all Mortgagee Letters and other instructions issued by HUD relating to the 203(k) Program, when undertaking any consultant function under the 203(k) Program.

(e) Complying with HUD's request for documentation relating to any 203(k) project on which the consultant has worked.

(f) Complying with HUD's monitoring requirements relating to the 203(k) Program.

PART 203—SINGLE FAMILY MORTGAGE INSURANCE

3. The authority citation for 24 CFR part 203 continues to read as follows:

Authority: 12 U.S.C. 1709, 1710, 1715b, and 1715u; 42 U.S.C. 3535(d).

4. Add § 203.50(l) to read as follows:

§ 203.50 Eligibility of rehabilitation loans.

* * * * *

(l) *Rehabilitation loan consultants.* HUD maintains a list of qualified consultants, in accordance with §§ 200.190 through 200.193 of this title. When the borrower elects to use the services of a consultant, the lender must select a consultant on the list to perform one or more of the following tasks:

(1) Conduct a preliminary feasibility analysis before or after the submission of a sales contract;

(2) Prepare the cost estimate, work write-up, and architectural exhibits required for the rehabilitation of the property;

(3) Conduct a plan review; and

(4) Conduct the draw inspections for the release of funds during the construction phase of the project.

Dated: July 8, 2002.

John C. Weicher,

Assistant Secretary for Housing—Federal Housing Commissioner.

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