

CONSTRUCTION LENDING

TRAINING MANUAL

PREFACE

This manual was designed as a basic training instrument to provide typical policies, practices and procedures used by financial institutions in the United States when originating and servicing loans to finance housing construction. It has been made relevant to the Mortgage Fund Program by indicating specific references in the Procedural Mortgage Lending Guide and the Mortgage Fund Operations Manual. If forms have been developed for the requirements of the program, they are provided and indicated with the symbol "_". Many of the forms are contained in the application, but are provided in addition as exhibits to facilitate the use of this manual.

CONTENTS

SECTION I : **CREDIT POLICY**

SECTION II : **LOAN ORIGINATION**

SECTION III : **LOAN ADMINISTRATION**

SECTION I

Real Estate Credit Policy

LAND, SITE DEVELOPMENT & HOME CONSTRUCTION

Loans for the acquisition of land, development of the site and construction of single-family homes.

CONTENTS	PAGE
1. Loan Committee	1
2. Loan Approval Authority	2
3. Loan Types.....	3
4. Loan Amounts.....	5
5. Loan Terms	6
6. Loan Pricing.....	7
7. Security	9
8. Disbursements	10
9. Repayment.....	12
10. Appraisals	13
11. Equity Requirements	14
12. Credit Criteria.....	15
13. Loans to One Borrower.....	16
14. Personal Guarantees	17
15. Legal.....	18
16. Commitments.....	19

17.	Documentation.....	20
18.	Title.....	21
19.	Insurance	22
20.	Underwriting Procedures.....	23
21.	Administration Procedures	24
22.	Regulatory Compliance.....	25
23.	Market Area	26
24.	Market Concentration	27
25.	Loan Type Concentration.....	28
26.	Loan Production Objectives.....	29
27.	Form of Request for Loan Approval	30
28.	Management Reports	31
29.	Loan Review	32
30.	Project Inspectors	33

EXHIBITS

- A. Loan Committee Submission Form
- B. Comprehensive Memorandum to Accompany Loan Recommendation

1. Loan Committee

During the development period of this lending function, it is recommended that the Bank's existing loan approval committee be required to act on all loan requests for land acquisition, land development and home construction loans.

Requests for committee action should be in a form similar to that which is attached with this recommended policy and should be distributed to all committee members at least three days prior to the meeting.

It is also recommended that both the Real Estate Loan Department Manager and the originating Loan Officer attend the meetings to present the loan and answer questions asked by committee members.

2. Loan Approval Authority

During the development period of this function, it is not recommended that officer loan authorities be used to approve loan requests for acquisition, development and construction loans.

The Procedural Construction Lending Guide, June 1993

Section 6. Loan Approval and Closing

Mortgage Fund Operations Manual, October 5, 1993

Section 2.2.2.2 Loan Approval Authority

Section 3.6 Sub-project Approval Procedures

3. Loan Types

A. Land

It is recommended that loans for acquisition only be made for land which has been fully approved by all governmental agencies and for which the borrower has a plan approved by the government authority and the Bank for site development and the construction of homes. Loans should not be made for speculative land purchases unless other collateral sufficient to repay the Bank is also provided.

Financing for land should be provided only for immediate development requirements.

B. Development

For the purposes of this policy, this classification refers to physical improvements to the land such as the installation of sewer, water, curbs and streets. Typically, the development phase refers to the cost associated with securing all approvals to allow construction on the land. Prior to acquiring a land loan from the Bank, the developer will either pay to have the land fully approved for development or purchase land which the seller has had approved. The developer can be given credit toward his equity for cost he has paid to secure all required approvals.

Before receiving a loan to finance the installation of the aforementioned improvements, the borrower must provide the Bank with a complete budget indicating all costs. The costs must be verified by contracts for the purchase of material and labor and be confirmed further by a review conducted by the Bank's inspecting engineer.

Only improvements for the immediate home building requirements should be financed. If homes are to be built in phases, site improvements should be limited to only those homes for which the Bank is providing a construction loan and from the sales of which the development cost can be fully repaid.

In the case of both land and site improvements, if not immediately used, the cost of these items can be a significant drain on the developer's cash.

C. Construction

This loan can be a part of the previous two loan types or may stand alone, if the borrower has purchased fully-improved land and is using the land as its equity. In either case, the proceeds of this loan will be used to finance the construction of homes.

If the loan is being used to finance single-family homes, it is recommended that the borrower be allowed to build no more than two sample homes, each of a different design. In addition, the borrower may be permitted to maintain an inventory of no more than two homes -- one of each home type-- for immediate delivery to buyers.

Construction of the remaining homes should only be allowed when a purchaser has deposited the required down payment and been approved for a mortgage.

With respect to down payments of purchasers, these funds should be closely monitored by the Bank. All deposits should be deposited in an escrow account with the bank and should not be available to the borrower for construction or to be taken as profit.

If the homes to be constructed are attached (townhomes or flats), it is, of course, necessary to complete a group of homes. In this case, 80% of the group should be sold before the next group is started.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.2.1 Eligible Sub-projects

4. Loan Amounts

A. Land

Not in excess of 40% of cost, including the cost to get the property approved for development. If an appraisal of the property indicates the value to be less than the cost, the loan amount should not exceed 40% of the appraised value.

B. Development

Not in excess of 50% of the actual cost to install site improvements.

C. Construction

Lesser of 75% of the cost (for actual construction [hard cost] and interest, legal, loan fees, taxes, insurance, miscellaneous [soft cost]) or appraised value.

The Procedural Construction Lending Guide, June 1993

Section 5.3 Commercial Space Construction

Section 5.4 Single Family Construction

Mortgage Fund Operations Manual, October 5, 1993

Section 3.3.4 Maximum Loan Amount

5. Loan Terms

A. Land

Not in excess of six months with option to extend for an additional six months, provided evidence is given to the Bank that development will definitely start during the extension period.

B. Development

Not in excess of one year. The term will be governed by the size of the project and site conditions.

C. Construction

Maximum of 18 months for single-family and 24 months for multi-family.

NOTE: It is recommended that the Bank not provide financing for any development that cannot be completed within two years. This limitation is suggested to protect against increases in costs due to labor, material and interest rates.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.5.2 Repayment and Maximum Loan Term

6. Loan Pricing

A. Interest Rates

Land Development and Constructions loans are priced at a variable rate, based on the current basic rate of the National Bank of Poland.

Mortgage Fund Operations Manual, October 5, 1993

Section 1.5.1 Interest Rate Policy

Section 3.5.1 Interest Rate

Section 3.5.3 Capitalization of Unpaid Interest

B. Fees

A 1% non-refundable application fee for all loans, plus the following:

i. Land

A minimum of 3% of the loan amount, not refundable, to be paid when the commitment is issued.

ii. Development

A minimum of 2% of the loan amount, not refundable, to be paid when the commitment is issued.

iii. Construction

A minimum of 1% of the loan amount, not refundable, to be paid when the commitment is issued.

7. Security

- A. For all loans, a first lien on land and existing or to-be-built improvements.
- B. Secondary personal guarantees, if appropriate.

Mortgage Fund Operations Manual, October 5, 1993

Section 1.5.5 Legal Policies

Section 3.4.2 Collateral Requirements

Section 3.4.3 Collateral not to be Excessive

8. Disbursement

A. Land

Funds needed in excess of equity to be funded at loan closing.

Any amounts to be used for approvals, improvements, etc., are to be advanced when borrower presents bona fide bills or receipts for payment.

B. Development and Construction

Payment for the installation of site improvements and construction of homes to be made in accordance with budgets approved by Bank. Disbursements for the construction of homes may be made in either of two methods:

Method 1 is the Stage Payment Procedure. In this method, a house is sectioned into four to eight parts and the amount to be advanced at the completion of each part is pre-determined. As each section is completed, as verified by the inspector, payment is made.

Method 2 is the Percentage of Completion method. With this method, the borrower requests payment for all work completed and materials installed at the date of the request. The inspector reviews the work, and, if in agreement, approves it for payment.

As noted, each method relies on the inspector. The first method usually has fewer draws during the loan and in some respects is easier to administer.

Requests for payments should be made at least one week prior to required dates for payments to contractors and material suppliers. Requests are to be on a form provided by or approved by the Bank. All payments will be subject to retainage of not less than 10%. Retainage will be released within 30 days after contractor and material suppliers have completed their contracts to the satisfaction of the Bank. Retainage is not always required for home construction, but it is recommended.

Payments by the Bank will be made not more often than every two weeks.

The Bank may either make payment to the borrower or to the contractor and materials suppliers.

If the Bank pays the borrower, it must receive proof prior to the next disbursement that all contractors and material suppliers have been paid in the amounts for which they requested payment, less the retainage.

Mortgage Fund Operations Manual, October 5, 1993

Section 3.7.3 Disbursement of Proceeds From the Bud Bank

Section 3.8.3 Bank Disapproval of Loan Disbursement Requests

Section 3.8.4 Bud Bank's Disapproval of Funding Requests

Section 2.2.2.4 Disbursement of Loan Proceeds

9. Repayment

A. Land

The borrower may either sell lots to others or may construct homes and sell them. In either case, the objective of the Bank is to get its land loan repaid as quickly as possible and reduce its exposure.

When the lot is to be released as the result of a sale, the loan should be repaid at a rate of not less than 125% of the pro-rata amount of the loan.

B. Development and Construction

As with land loans, the Bank's objective is to reduce its exposure as quickly as possible. When a house is sold, the loan should be repaid at a rate of not less than 110% of the pro rata loan amount or 90% of the sales price, whichever is greater.

This procedure, in effect, defers the borrower's profit, giving it plenty of incentive to complete the project. The Bank, with this procedure, is usually out of the project with the sale of the home, which represents approximately 70% to 85% of the total houses in the project.

10. Appraisals

While appraisals are recommended, they may not be readily available. It is therefore recommended that equity requirements be sufficient enough to provide a substantial loan to cost margin.

The Bank should determine which appraisers are reliable and approve their qualifications in order to use them when possible. When appraisals are used, they should be contracted for by the Bank by giving specific, written instructions as to the purpose of the appraisal. Although the borrower must pay for the appraisal as part of the cost to obtain the loan, the appraisal is entirely for the benefit of the Bank, and it makes no representation of value to the borrower.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.6.2 Current Values

11. Equity Requirements

Equity must be injected by the borrower for all three types of loans. As noted under the "Loan Amount" section of this policy, the Bank will have specific limits as to how much it will loan for each type of loan.

Equity requirements can be satisfied by the borrower contributing land, money, paying for construction cost, cost to obtain approvals, or any combination, which can be verified by the Bank and which satisfies the Bank.

[Removed NOTE]

Mortgage Loan Operations Manual, October 5, 1993
Section 3.3.5 Types of Equity

12. Credit Criteria

The essential standards focus on the following for borrower and guarantors:

- Integrity
- Substantial, verifiable financial resources
- Experience
- Knowledge

The loan officer's report should provide evidence of the above points with documented investigative information.

Mortgage Fund Operations Manual, October 5, 1993

Section 3.2.3 Eligible Beneficiaries

Section 3.2.4 Ineligible Beneficiaries

13. Loans to One Borrower

A limit should be applied as to how much real estate loan credit can be provided to any one borrower whether direct or contingent obligations.

14. Personal Guarantees

Whenever possible, guarantees should be required. The investigation of guarantor should be the same as that conducted for direct obligors.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.4.3 Collateral not to be Excessive

15. Legal

It is suggested that during the development stages of this function and until government and other regulatory agency requirements are generally known and understood, a legal representative should review loans being submitted for approval.

The legal representative should opine as to compliance with known requirements and compliance to the Bank's credit policy. All commitment letters and documents required by the Bank should be prepared by the legal representative.

The cost for the Bank's legal representative should be paid by the borrower.

16. Commitments

Borrower should be advised of the loan approval by a commitment letter which is prepared by the Bank's legal representative. The commitment letter should reflect the terms and conditions presented to and approved by the Loan Committee. All requirements necessary to close the loan should be fully explained and specific instructions given to the borrower as to its responsibilities and obligations.

The borrower should be required to sign the commitment letter and return a copy to the Bank, together with required fees. A specific date by which the commitment must be returned should be stipulated.

The commitment letter should also be specific as to how long the commitment will last.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.6.4 Commitment Letter

17. Documentation

All aspects of the loans should be documented, including application, various investigation and verifying information obtained during the underwriting processes, to the commitment and legal loan documents.

Legal documents should be prepared by the Bank's legal representative, who should make sure the Bank receives the original of each document and also should follow for the receipt of any documents which are not immediately available after the loan closing.

Legal documents should be maintained in a fire-proof, secured area to be accessed only by authorized personnel.

The Procedural Construction Lending Guide, June 1993

Section 6.1 Loan Agreement

Mortgage Fund Operations Manual, October 5, 1993

Section 3.6.5 Construction Sub-loan Agreement

18. Title

The legal representative should be responsible for investigating the status of title of the real estate being taken as collateral for loans.

There should be a legal opinion that the Bank has a first lien on the property and that there are no taxes outstanding or any other existing conditions which would impair the Bank's position.

Any exceptions to title condition must be approved by a senior officer of the Bank with the counsel of the Bank's legal representative as to the possible risk to the Bank in making an exception.

Mortgage Fund Operations Manual, October 5, 1993
Section 1.5.5 Legal Policies
Section 3.4.2 Collateral Requirements

19. Insurance

The originating loan officer should obtain a policy of insurance protecting the Bank's interest in the property against loss due to fire or any other catastrophe against which insurance is normally provided.

The cost for insurance is to be paid for by the borrower.

The administrative section must monitor the adequacy of coverage during the term of the loan.

The Procedural Construction Lending Guide, June 1993
Section 8.1 Hazard Insurance Loss

20. Underwriting Procedures

The detailed procedures for underwriting land acquisition, land development and home construction loans are an integral part of the credit policy.

The required procedures should be complied with in all respects and any digression should be approved by the Loan Committee.

The loan recommendation presented to the Committee by the originating loan officer should provide a complete disclosure of all information known to the originating officer, and, in general, should provide evidence that the officer has a thorough understanding of the credit.

As noted under the previous legal section, it is suggested that the Bank's legal representative opine that the loan complies with the Bank's loan policy.

The Procedural Construction Lending Guide, June 1993

Section 5.1 Credit Analysis

Section 5.1.1 Community Associations -- Additional Information

Section 5.1.2 Project Analysis

Section 5.1.3 Properties Affected by Environmental Hazards

Section 5.2 Loan Underwriting

Mortgage Fund Operations Manual, October 5, 1993

Section 3.6 Sub-project Approval Procedures

21. Administration Procedures

The detailed procedures governing the administration of land acquisition, land development and home construction loans are an integral part of the credit policy.

In order to protect the Bank and its assets against possible loss, it is essential that all loans be administered in strict accordance with the terms and procedures approved by the Loan Committee.

Any occurrence which indicates a possible deterioration in the quality of the loan must immediately be reported to the Loan Review Committee with specific details as to the condition of the loan and the remedial action taken or proposed.

It will then be the decision of the Loan Review Committee as to what other reporting is appropriate.

Procedural Construction Lending Guide, June 1993
Section 7 Construction Loan Servicing Procedures

22. Regulatory Compliance

As noted under the previous Legal section, it will be the responsibility of the Bank's legal representative to be sure that transactions contemplated conform in all respects with government and other regulatory requirements.

Mortgage Fund Operations Manual, October 5, 1993

Section 3.4.1 Local Regulations and Requirements

Section 3.9.4.1 Legal Requirements

23. Market Area

The Bank should specify and accordingly notify the Real Estate Loan Department of any geographic areas which for any reason it will not provide land acquisition, land development or construction loans.

24. Market Concentration

The Bank should be careful not to provide financing overly concentrated in any one area. This is to avoid repercussions from economic changes in an area that could result in a deterioration of loan quality.

It should also be careful not to provide loans for projects which will be in direct competition with other projects financed by the Bank. A slowness in market acceptance of the projects could possibly cause loan quality deterioration.

25. Loan Type Concentration

The Bank should not become overly committed in loans of one type, but should take the necessary steps to assure that its risk is spread.

26. Loan Production Objectives

The Bank management, on a regular basis, should provide the Real Estate Loan Department with objectives for loan production, indicating desired loan types, maturities, yields and credit criterion.

27. Form for Request of Loan Approval

The Loan Committee should approve a standard form which is to be used for all land acquisition, land development and home construction loans being presented for Loan Committee action.

It is recommended that the report be in two parts, similar to the attached example.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.6 Sub-Project Approval Procedures

28. Management Reports

The Real Estate Loan Department should be required to provide, on a monthly basis, at least the following reports:

1. Loans outstanding
2. Commitments outstanding
3. Loans in process
4. Delinquent or problem loan status
5. Year-to-date loan production
6. Year-to-date income (interest and fees)
7. New business efforts

Mortgage Fund Operations Manual, October 5, 1993

Section 2.1.2 Reporting Requirements

Section 2.2.2.7 Reporting Requirements

29. Loan Review

The Real Estate Loan Department loans should be monitored by the Loan Review Department for compliance with administrative procedures and loan quality. This procedure can be random, but all loans should be reviewed on a quarterly basis to help prevent any unwanted surprises.

30. Project Inspections

The bank should select several construction inspectors. The credentials of each, indicating their respective experiences and verification of integrity, should be presented to the Loan Committee. Only those inspectors approved by the Committee should be used to provide cost verifications and make inspections for construction advances.

Assignments should be made in writing, stating specifically the duties and responsibilities of the inspector.

The cost for inspection services should be paid by the borrower. BUT the inspector's reports and representations of the inspectors are entirely for the Bank's benefit. By approving work for payment, the inspector is not making any representation to the borrower or any other party as to the quality of construction, adherence to plans and specifications or any other matters.

Construction Fund Operations Manual, October 5, 1993

Section 2.2.2.5 Monitoring the Progress of Construction Funds

Section 3.9 Supervision of Construction

EXHIBITS

EXHIBIT A

(Loan Committee Submission Form)

[BORROWER NAME]

[ADDRESS]

PROPOSED COMMITMENT:

PURPOSE:

TERMS OF REPAYMENT:

RATE:

FEES:

BORROWER:

GUARANTOR:

SECURITY:

PRESENT INDEBTEDNESS:

RELATED LOANS:

OTHER RELATIONSHIPS WITH THIS BANK:

AVERAGE DEPOSIT BALANCES:

FINANCIAL STATEMENTS:

	<u>Borrower</u>	<u>Guarantors</u>
	Date	Date
Cash		
Receivable		
Interest in Real Estate		
Total Assets		
Total Liabilities		
Net Worth		

(Note: it should be indicated whether the statements are audited, accountant-prepared, personal, etc.)

CREDIT POLICY EXCEPTION: NO / YES
(If YES, explain and indicate authority, who approved exception.)

RECOMMENDATION BY: _____ **Date:** _____

CREDIT OFFICER:

MANAGER:

SPECIAL TERMS OR CONDITIONS:

COMMENTS:

EXHIBIT B

(Comprehensive Memorandum to accompany Loan Recommendation)

[BORROWER NAME]

[ADDRESS]

I. THE REQUEST

- Amount
- Loan Term

II. PROJECT DESCRIPTION

- Location
- Unit types and mix
- Type of construction

III. BORROWER

- Current business
- Previous business experience
- Who are principals?
- Summary of financial condition
(attach complete financial statements as exhibit)

IV. GUARANTORS

- Same information as for Borrower

V. SOURCE AND USE OF FUNDS

- Hard cost
- Soft cost

- Equity
- Credit

VI. PROJECT PERFORMANCE

- Assumption of sales activity
- Cash flow

VII. INTEREST AND OPERATING RESERVE ANALYSIS

- Calculation of interest reserve
- Calculation of operating reserve

VIII. REPAYMENT ANALYSIS

- Release prices
- Projection of when credit will be repaid

IX. MARKET ANALYSIS

- Comparable homes and average value
- New construction in the area

X. VALUE OF COLLATERAL

- Appraisal information
- Who performed appraisal?

XI. CONTRACTOR

A. Background

- Business history and experience

B. Financial Statements

- Summary of financial condition
(attach financial statement as exhibit to this memo)

Name

Date

Cash

Receivables

Interest in real estate

Total assets

Total liabilities

Net worth

(Note: indicate type of statement-audited, accountant-prepared, personal, etc.)

XII. CREDIT RISKS

- List all known possible risks

XIII. CREDIT STRENGTHS

- Comments
- Recommendations

XV. EXHIBITS

[List] Financial Statements
Maps
Photographs
Etc.

SECTION II

Construction Loan Origination

TABLE OF CONTENTS

	Page
PREFACE	1
I. LOAN ORIGINATION.....	2
II. UNDERWRITING 4	
A. Project 4	
1. Land 4	
2. Site Development and Home Construction.....	5
a. Plans, Specifications and Costs Breakdown.....	5
b. Site, Location and Market	7
B. Repayment 11	
C. Borrower 11	
D. Guarantor 12	
E. Contractors 13	
III. LOAN APPROVAL REQUEST	14
IV. LOAN COMMITTEE PRESENTATION.....	15
V. COMMITMENT 16	
VI. PRECEDENCE TO CLOSING.....	17
VII. LOAN CLOSING	18
VIII. POST-CLOSING.....	19
IX. EXHIBITS [- Mortgage Fund Program Forms]	
A Applications	

- A-1 _Multi-Family
- A-2 _Single-Family
- B Application Register
- C Worksheet
- C-2 _Worksheet
- D Conversation Sheet
- E Letter of Acknowledgment
- F Letter of Instruction to Inspecting Engineer
- G Letter of Instruction to Appraiser
- G-1 _Letter of Instruction to Appraiser
- H _Environmental Information
- I _Site Inspection Report of Engineer
- J _Costs Breakdown
- K _Market Analysis
- L _Potential Unit Buyers
- M _Bidding Requirements
- N _Contractor Information
- O Loan Presentation
- P Comprehensive Memorandum
- Q Letter of Commitment

PREFACE

The financing of construction is a form of real estate lending which requires the application of highly specialized underwriting and administrative skills.

Since there is a high degree of risk associated with this activity, it is essential to keep such risk at a minimum by adhering to prudent Bank-approved underwriting standards and diligent administrative practices.

While policies and procedures will of necessity from time to time change, until such change occurs all loans must be originated in accordance with the existing regulations. Any warranted exceptions to these regulations must be approved by the Bank's management before an exception can be permitted.

I. LOAN ORIGINATION

The credit officer should meet with the applicant to discuss the proposed land acquisition or housing project. The developer should be questioned extensively as to why he has selected the subject site and why he believes the type of houses or flats to be built will appeal to purchasers.

If, after an extensive discussion about the project and the builder's background and experience, the credit officer believes there is a good probability that the Bank can make a loan for the subject project, a loan application [Exhibits A-1 & A-2] can be provided to the developer. The developer should be informed of the terms and conditions the Bank requires for loans of the type under consideration, which include loan amount, interest rate, term, repayment provisions, and all fees which the developer must pay. The credit officer should review the application with the developer and give instructions that all indicated information must be provided completely by a specific date to enable the Bank to provide a decision by a specific date.

The applicant should also be advised of any fees which must accompany the application to cover the cost of any expenses to be incurred by the Bank in processing the application.

The detailed interview process and the required application fee will help eliminate time spent evaluating unworthy credit requests.

When the credit application is received, the credit officer must respond immediately, and pursue the underwriting diligently to obtain the Bank's decision.

Upon receipt of the completed application, together with the fee and required documents, the request should be dated, entered into the Application Register [Exhibit B], and assigned a processing number. A worksheet [Exhibit C] should be started and the estimated decision date indicated in the register and on the worksheet. From the time of initial contact until the loan is repaid, conversations with the applicant/borrower should be documented [Exhibit D]. A form letter [Exhibit E] should be sent to the applicant acknowledging receipt of the application and fee and indicating the estimated time for a decision.

Mortgage Fund Operations Manual, October 5, 1993

Section 3.6.1 Submission of Application

Section 3.5 Sub-loan Terms and Conditions

II. UNDERWRITING

The underwriting process requires collecting and analyzing all pertinent information about the project, the borrower, guarantors, and any other relevant information about the credit.

A. The Project

The analysis of the security for the credit is a joint effort to be headed by the credit officer with the assistance of a Bank-appointed inspecting engineer and a Bank-appointed appraiser.

The credit officer will assign specific duties to the respective agents. Assignments are to be made in writing [Exhibits F, G & G-1], indicating in detail what is expected from each one and setting a date by which their reports must be provided to the Bank.

Following are the procedures to be used to analyze the security being pledged for the credit:

1. Land

A land loan should only be considered when the land has been fully approved by all controlling authorities, development of site improvements and the construction of homes will commence within six months from the date the loan is approved, and the amount of land can be fully improved with homes within two years from the date the loan is approved. The only exception to this policy would be if other liquid assets are provided as security which can be used to repay the acquisition loan at maturity if the loan has not been repaid from the construction and sale of homes.

When underwriting the land acquisition loan, the credit officer must obtain a copy of the fully-executed purchase agreement, obtain copies of all zoning and building approvals, environmental approvals [Exhibit H], confirmation of plans and cost for the development of the site. Property information should be given to the appraiser with specific written instructions for the assignment. The appraisal report should be in a Bank-approved format, indicating the appraiser's estimate of value based on the following:

- highest and best use;
- proposed use of the land; and
- comparison to the value of other properties in the area

which have sold within the past year.

Information relating to the site improvements, including all plans and costs, should be given to the inspecting engineer for approval and verification of projected costs for site improvements.

Mortgage Fund Operations Manual, October 5, 1993

Section 3.3.2 Land Status and Costs

Section 3.4.1 Local Regulations and Requirements

2. Site Development and Home Construction

To properly determine if the project is suitable for the requested loan, the following procedures must be completed:

a. Plans, Specifications and Cost Breakdowns

The credit officer should make a preliminary review for completeness and become familiar with the design and size of the product. All of this information should then be given to the inspecting engineer who should carry out a complete analysis [Exhibit I], evaluating the following:

- costs breakdown [Exhibit J];
- completeness of plans and specifications;
- quality of materials;
- compliance to building codes and zoning requirements;
- construction can be completed based on costs projected by the developer;
- compliance with environmental requirements;
- utilities available to the site;
- construction procedures are correct for the proposed buildings;
- verification of soil conditions and the appropriateness of footings and foundation design based on soil conditions; and
- terms and conditions of fixed price contracts for contractor and subcontractors.

During the course of construction, the inspector must ensure that the Bank is protected from loss as a result of the developer or his contractor failing to adhere to any of the requirements of the Bank, practices which were approved during the underwriting process or building or zoning codes. The inspector will be required to approve work as it is installed and to approve all requests for progress payments.

The plans, specifications and cost information should also be given to the appraiser with specific written instructions for the assignment. The appraisal report should be in a Bank-approved format indicating the appraiser's estimate of value based on the following:

- highest and best use of the property;
- homes to be built;

- proposed sales prices;
- quality of materials to be used and construction procedures;
- comparison to the value of other properties in the area of the subject;
- estimate of time to sell;
- analysis of cost to construct; and
- cost of land.

The appraisal report should substantiate each of the foregoing.

b. Site, Location and Market

The credit officer, having reviewed the site development and house plans, and being aware of the proposed sales prices of the homes, should now visit the property as an initial step in conducting a market study. This visit can coincide with the preliminary visit being made by the Bank-appointed appraiser. The credit officer should pay attention to the proposed layout of houses on the site, the location of streets, the market area, particularly whether the site is in a predominately residential area, which will attract purchasers. The inspection should include noting the adequacy of highways and public transportation to provide good access to employment and shopping areas, location of schools, and other prominent facilities such as banks, hospitals, etc.

It should also be noted whether the site is located in an area subject to flooding, which could adversely affect the salability of the homes.

The collective information from the credit officer's inspection of the site and analysis of the market [Exhibit K] and the reports of the appraiser and the inspector should provide the credit officer with substantial knowledge about the credit security.

The borrower should provide a list [Exhibit L] of potential unit buyers.

Mortgage Fund Operations Manual, October 5,1993
Section 3.3.4 Sales of Housing Units

The credit officer must now turn attention to the sources and uses of funds. Beginning with the uses, the following must be analyzed. First, the "Hard" or "Direct" costs, including:

- Land
- Site improvements (streets, curbing, water and sewer)
- Construction components (footings, foundation, framing, roofing, electrical, plumbing, masonry, carpentry, painting, landscaping, paving, contingency reserve, etc.)

Second, the "Soft" or "Indirect" costs, including:

- Legal fees, loan fee, architect's fees, real estate taxes, insurance, marketing fees, appraisal fees, inspection fees, contingency reserve, developer's fee, and interest on the loan.

Mortgage Fund Operations Manual, October 5,1993
Section 3.3.7 Construction Costs

The total of the direct and indirect costs make up the total project cost. Of these costs, a bank-specified minimum must be contributed by the developer as his equity. It does not make any difference which items the developer pays for, so long as the credit officer can verify the developer has actually paid the sums which amount to the required minimum costs.

If the items to be paid for by the developer are not paid prior to the injection of loan funds, then the credit officer must require that the money not contributed but due to be contributed be placed in an escrow account with the Bank at closing. This account can be under the joint control of the Bank and the developer.

Mortgage Fund Operations Manual, October 5,1993
Section 3.3.5 Types of Equity

The proceeds of the Bank loan can be funded on either a "stage" basis or on a "percentage of completed work" basis. The stage basis is predicated on each house being segregated into 4 to 8 parts. As each part is completed, as verified by the Bank's inspector, loan funds will be advanced to pay for that stage.

The percentage of completed work basis will schedule payments being made on a weekly or every two week basis for work completed as verified by the Bank's inspector. The procedure selected is a negotiated matter, either one being acceptable. Whichever method is used, evidence of payments to contractors, subcontractors and material suppliers must be verified. Verification can be accomplished by providing forms prepared by the Bank for trade or suppliers being paid. Each should sign and return it to the Bank. Successive payments should not be made unless confirmation of previous payments has been received by the Bank. Additional information concerning loan advances are included in the Administrative Procedures.

When analyzing the costs, all items should be substantiated by the developer with bona fide bids for materials and fixed-price contracts for the labor¹. The only exceptions should be the interest reserves, which will be estimated by the developer after consultation with the credit officer. The interest will be estimated based on the expected average loan balance outstanding during the loan term and the estimated average interest rate during the loan term.

¹Mortgage Fund Operations Manual, October 5, 1993
Section 3.2.118

If competitive bidding is required by the Mortgage Fund Program for awarding contracts Form BW-05 [Exhibit M] should be completed by the borrower.

The other items which cannot be confirmed are the contingency reserves for hard costs, and the contingency or operating reserves for soft costs. These

reserves can vary from 5% to 15% of total cost and are used to pay for increases in the project costs caused by construction changes approved by the Bank or can be used for interest if the interest reserve is depleted due to a substantial unforeseen increase in interest rates.

During the loan term, the loan administrator must be careful that contingency reserves are not drawn down too early in the loan term and any use of the contingency funds must be approved by the Bank before the developer incurs the additional cost. The funds are not to be used for cost increases which are the responsibility of the developer to contribute with additional equity.

When the credit officer is satisfied that all costs are appropriate, the source of funds must be established, based on the appraised value which is predicated on all houses being sold at an average price per house. The average is determined by assuming the number of each type of home to be built and the length of time it will take to completely sell out.

After considering the costs, with adjustments for interest and contingencies, the expected gross sales and the expected time to sell, the credit officer can negotiate the loan amount with the developer. When the loan amount is established, the developer must provide evidence of his capability to contribute the required equity.

Mortgage Fund Operations Manual, October 5, 1993

Section 3.2.8 Competitive Bidding Requirements

Section 3.3.1 Eligible Sub-Project Costs

Section 3.3.2 Land Status and Costs

Section 3.3.3 Costs Recovery and Sales Price

Section 3.3.7 Construction Costs

B. Repayment

The credit officer must set repayment terms to get the credit risk reduced as quickly as possible. The first proceeds from land release and/or the sale of homes are to pay down the credit. Profit for the developer is derived from the sales after the credit is repaid.

For land loans, lot releases should require payment of not less than 125% of the pro-rata loan amount.

For development and construction loans, releases should require payment of the greater of 110% of the pro rata loan amount or 90% of the sales price.

Whichever method is used, the objective is to have the credit completely repaid, preferably from the sale of 70% of the homes, but not more than through the sale of 85% of the homes, accounting for 85% of the project revenue.

Mortgage Fund Operations Manual, October 5,1993 ***Section 3.5.2 Repayment and Maximum Loan Term***

C. The Borrower

To properly evaluate the borrower, the credit officer must develop a profile comprised of personal character, business history, credit history, financial condition, knowledge of and experience in developing the type of project to be financed by the Bank. This process involves a great amount of investigation and verification work. The developer must provide information on his business experience and references which must be contacted to confirm information provided. Banking references and creditors must also be contacted for confirmation. A representative number of projects completed by the developer should be inspected by the credit officer to determine the quality of workmanship and general success of the projects. The developer must convince the credit officer of his having the knowledge and experience to successfully complete the subject project. The credit officer should get a good sense of how the developer

conducts his business by reviewing the details of the construction progress, including contracts with contractors and subcontractors, and the management team.

A very important indication of the capability of the developer is the designation of a chief assistant who can manage and complete the project if the developer for any reason becomes incapacitated during development.

All of the information obtained about the developer must be documented and retained in the loan file.

To get an understanding of the developer's financial condition will require an analysis of financial statements, tax returns, and banking statements for the past three years.

Audited or accountant-prepared financial statements may not be available, and it will therefore be left to the credit officer to be sure the developer provides complete information. If the developer has other real estate or investment businesses, the credit officer should obtain and analyze all operating statements paying particular attention to working capital, cash flows and direct and contingent liabilities. In the analysis, the credit officer should confirm the adequacy of equity funds to be injected into the subject project and the existence of assets which can be readily liquidated if additional equity is required during construction.

Copies of all financial statements, credit officer spreadsheets, analysis, and comments should be retained in the credit file.

D. Guarantors

The process of evaluating guarantors should be the same as those conducted for the borrower.

E. Contractors

Although the contractor is not obligated on the debt, it nevertheless is a major element contributing to the success or failure of the project. Therefore, a thorough evaluation of the contractor must be performed. Credit history, business history, knowledge of and experience in constructing projects similar to the subject, are all areas which must be investigated and confirmed. Financial condition of the contractor is extremely important and the same analysis of financial condition as performed for the borrower must also be conducted for the contractor.

Subcontractor and material suppliers used by the contractor should be contacted and payment history confirmed. The Bank construction inspector can often be helpful in assisting in the investigation of the contractor. The required information is presented on a form [Exhibit N].

Procedural Construction Lending Guide, June 1993

Section 5.1 Credit Analysis

Section 5.1.1 Community Associations -- Additional Information

Section 5.1.2 Project Analysis

Section 5.1.3 Properties Affected by Environmental Hazards

Section 5.2 Loan Underwriting

III. LOAN APPROVAL REQUEST

Having assembled and analyzed information about the property, the project, the costs, the borrower, guarantors, contractors, and if believing this is a good credit opportunity, the credit officer is now in a position to prepare the presentation for the Loan Committee decision.

This presentation will be in two parts: the first will be an abbreviated form setting forth the specific terms and conditions of the loan and brief background information [Exhibit O]; the second part will be a comprehensive discourse providing information about all elements of the loan request [Exhibit P].

After providing all known information, the credit officer must then provide an analysis of risk or possible risks with strengths which outweigh the risks, thereby concluding why the credit is an acceptable investment for the Bank.

Procedural Construction Lending Guide, June 1993
Section 6 Loan Approval and Closing

Mortgage Fund Operations Manual, October 5, 1993
Section 3.6 Sub-Project Approval Procedures

IV. LOAN COMMITTEE PRESENTATION

The loan underwriting information which constitutes the request for Loan Committee action should be given to a legal representative who should opine that the loan conforms to all known regulating requirements and the Bank's credit policies. It should then be given to the real estate loan unit manager for review and concurring recommendation to the Loan Committee. The entire package of information should be distributed to each of the committee members at least three full business days prior to the meeting day.

The credit officer and the real estate loan unit manager should attend the Loan Committee meeting where the credit officer should make a verbal presentation to the committee summarizing his loan recommendation and answering relevant questions from committee members.

The presentation by the credit officer can include maps, pictures of the site and/or surrounding area, pictures or architects renderings of homes to be built, or any other exhibits which will assist in communicating relevant information about the project to the Loan Committee.

V. COMMITMENT

The credit officer should provide the Bank's legal representative with a copy of the Loan Committee presentation as approved. The credit officer should then meet with the legal representative and discuss the preparation of the commitment letter.

The legal representative should draft a letter for review and approval by the credit officer. The letter should be similar to the attached [Exhibit Q].

All requirements necessary to close the loan should be fully explained, and specific instructions given to the borrower as to its responsibilities and obligations.

The letter should specify the commitment period and the date by which the commitment must be signed by the borrower acknowledging its approval, and returned to the Bank with the commitment fee in the agreed-upon amount.

The letter should be signed for the Bank by an authorized officer.

The issuance of the commitment letter may not conclude negotiation between the developer and the Bank. For one reason or another, the terms and/or conditions may have to be changed. If this occurs, the credit officer must prepare a memorandum explaining the situation and request approval to make the necessary change or changes.

Depending on the limitation of authority existing in the department, the request for approval may have to be submitted to the Loan Committee.

Any changes should be reflected in an amended commitment letter prepared by the Bank's legal representative.

The final commitment letter will provide the framework for the loan documents, which will be prepared by the bank's legal representative.

Procedural Construction Lending Guide, June 1993
Section 6 Loan Approval and Closing

Mortgage Fund Operations Manual, October 5, 1993
Section 3.6.4 Commitment Letter

VI. PRECEDENCE TO CLOSING

The credit officer should advise the construction loan administration section of the loan approval. A copy of the signed commitment letter should accompany the advice along with the commitment fee. The administrative section will be responsible for establishing accounts for any fees or equity funds which will be disbursed during construction.

The administrative section personnel should review the loan terms and conditions and advise the credit officer of any requirements they have which must be satisfied before the loan closing. It is the credit officer's responsibility to communicate such matters to the borrower and Bank's legal representative, if necessary.

The Bank's legal representative should prepare all loan documents required by the Bank. The documents should be reviewed by the credit officer and the loan administration unit manager before they are sent by the Bank's legal representative to the developer or its legal representative.

Procedural Construction Lending Guide, June 1993

Section 6.1 Loan Agreement

Mortgage Fund Operations Manual, October 5, 1993

Section 3.6.5 Construction Sub-Loan Agreement

VII. LOAN CLOSING

At the closing, which should be carried out under the supervision of the Bank's legal representative, borrower will be required to sign all documents required by the Bank, deliver any equity funds to be held by Bank, and pay any fees or costs associated with the closing including legal, appraisal, and inspection fees.

The borrower and the Bank should sign two sets of final plans and specifications which have been reviewed and approved by the Bank's construction inspector. No construction changes can be made without the Bank's approval.

Procedural Construction Lending Guide, June 1993
Section 6 Loan Approval and Closing

VIII. POST CLOSING

The credit officer should deliver the loan file, the signed plans and specifications, and all executed loan closing documents to the administration unit. There may be documents, one of which will be the mortgage, which must be recorded and will not be available until some time after the closing. The legal representative and the administrative unit should follow to receive any missing documents.

The credit officer will now yield to the assigned administrator, who will oversee the loan on a daily basis. In the event of any problems, the credit officer should be informed and his assistance required in dealing with the borrower.

EXHIBITS

EXHIBIT O

(Loan Committee Submission Form)

[BORROWER NAME]

[ADDRESS]

PROPOSED COMMITMENT:

PURPOSE:

TERMS OF REPAYMENT:

RATE:

FEES:

BORROWER:

GUARANTOR:

SECURITY:

PRESENT INDEBTEDNESS:

RELATED LOANS:

OTHER RELATIONSHIPS WITH THIS BANK:

AVERAGE DEPOSIT BALANCES:

FINANCIAL STATEMENTS:

	<u>Borrower</u>	<u>Guarantors</u>
	Date	Date
Cash		
Receivable		
Interest in Real Estate		
Total Assets		
Total Liabilities		
Net Worth		

(Note: it should be indicated whether the statements are audited, accountant-prepared, personal, etc.)

CREDIT POLICY EXCEPTION: NO / YES
(If YES, explain and indicate authority, who approved exception.)

RECOMMENDATION BY: _____ Date: _____

CREDIT OFFICER: _____

MANAGER: _____

SPECIAL TERMS OR CONDITIONS:

COMMENTS:

EXHIBIT P

(Comprehensive Memorandum to accompany Loan Recommendation)

[BORROWER NAME]

[PROJECT NAME]

I. THE REQUEST

- Amount
- Loan term

II. PROJECT DESCRIPTION

- Location
- Unit types and mix
- Type of construction

III. BORROWER

- Current business
- Previous business experience
- Who are principals?
- Summary of financial condition
(attach complete financial statements as exhibit)

IV. GUARANTORS

- Same information as for borrower

V. SOURCE AND USE OF FUNDS

- Hard cost
- Soft cost

-
- Equity
 - Credit

VI. PROJECT PERFORMANCE

- Assumption of sales activity
- Cash flow

VII. INTEREST AND OPERATING RESERVE ANALYSIS

- Calculation of interest reserve
- Calculation of operating reserve

VIII. REPAYMENT ANALYSIS

- Release prices
- Projection of when credit will be repaid

IX. MARKET ANALYSIS

- Comparable homes and average value
- New construction in the area

X. VALUE OF COLLATERAL

- Appraisal information
- Who performed appraisal?

XI. CONTRACTOR

A. Background

- Business history and experience

B. Financial Statements

- Summary of financial condition
(Attach financial statement as exhibit to this memo)

Name

Date

Cash

Receivables

Interest in real estate

Total assets

Total liabilities

Net worth

[Note: indicate type of statement—audited, accountant-prepared, personal, etc.]

XII. CREDIT RISKS

- List all known possible risks

XIII. CREDIT STRENGTHS

- List all known strengths

XIV. SUMMARY

- Comments
- Recommendations

XV. EXHIBITS

[List] Financial Statements

Maps

Photos

Etc.

EXHIBIT E

(Application Acknowledgement)

[Date]

Name
Address

RE: Project Name
Location

Dear _____:

This letter is to confirm our receipt of your credit application in the amount of \$_____ together with the application fee in the amount of \$_____.

If your request is approved, the proceeds of the credit will be used to finance construction of the subject which will be the security for the credit.

Your application is being processed, and we expect to advise you with respect to approval by [Date]. If we find that we need additional information to complete the processing, we will contact you. If processing is delayed and we cannot have a decision by the date indicated above, we will advise you accordingly.

We appreciate the opportunity to be of service.

Very truly yours,

--	--	--	--	--	--	--	--	--

**CONSTRUCTION LOAN
UNDERWRITING WORKSHEETS
AND DOCUMENT CHECKLISTS**

Project: _____ Credit Officer: _____

Application Received: _____
(date)

Request Decision by: _____
(date)

BANK AGENTS:

Appraiser: _____ Appt'd: _____ Rpt. Due: _____ Rec'd: _____
(date) (date) (date)

Address: _____ Appraisal reviewed and approved

Phone: _____ by: _____
(name) (date)

Inspecting _____
Engineer: _____ Appt'd: _____ Rpt. Due: _____ Rec'd: _____
(date) (date) (date)

Address: _____ Report reviewed and approved

Phone: _____ by: _____
(name) (date)

Legal _____
Representative: _____

Address: _____

Phone: _____

APPLICANT'S AGENTS:

Architect: _____

Address: _____

Phone: _____

Contractor: _____

Address: _____

Phone: _____

Legal Rep.: _____

Address: _____

Phone:



FEES:

Application (non-refundable): \$ _____ Rec'd: _____

Commitment: \$ _____ Rec'd: _____

Appraisal: \$ _____ Rec'd: _____

Inspecting Engineer: \$ _____ Rec'd: _____

Legal: \$ _____ Rec'd: _____

Other: \$ _____ Rec'd: _____

Application Confirmation Sent: _____ (date) _____

Loan Committee Action _____ (date) _____

APPROVED: _____ DECLINED: _____

Comments: _____

Commitment Letter Sent: _____ (date) _____

Signed Commitment Letter due from Applicant: _____ (date) Rec'd: _____ (date)

Loan Closed: _____ (date)

Loan File delivered to Loan Administrator: _____ (date)

ATTACHMENTS:

- Application Document Checklist
- Pre-Closing Document Checklist
- Project Analysis
- Borrower and Guarantor Financial Analysis
- Interest Reserve Analysis

- Site Inspection Report of Credit Officer

APPLICATION DOCUMENT CHECKLIST

PROJECT	Received
• Plans and Specifications	<input type="checkbox"/>
• Costs Breakdown	<input type="checkbox"/>
• Evidence of Land Purchase Price	<input type="checkbox"/>
• Current City Map	<input type="checkbox"/>
• Current Zoning Map	<input type="checkbox"/>
• Construction Contract –fixed price	<input type="checkbox"/>
• Feasibility Study	<input type="checkbox"/>
• Evidence of Utilities (water, sewer, gas, electricity)	<input type="checkbox"/>
BORROWER AND GUARANTOR	
• Financial Statements	Yrs. ___ ___ ___ B:___ G:___
• Background and Experience	B:___ G:___
• Bank References	B:___ G:___
• Business References	B:___ G:___
• Tax Returns	Yrs. ___ ___ ___ B:___ G:___
• Evidence of Equity	B:___
CONTRACTOR	
• Financial Statements	Yrs. ___ ___ ___ <input type="checkbox"/>
• Background and Experience	<input type="checkbox"/>
• Bank References	<input type="checkbox"/>
• Business References	<input type="checkbox"/>

PRE-CLOSING DOCUMENT CHECKLIST

- TITLE INFORMATION AND CLEARANCE
- SURVEY
- FINAL PLANS AND SPECIFICATIONS
- SOILS REPORT
- BUILDING PERMIT
- APPRAISAL
- CERTIFIED COST BREAKDOWN WITH CONTRACTS, BIDS, ESTIMATES, ETC.
- EVIDENCE OF COMPLIANCE WITH ZONING
- INSURANCE (AS REQUIRED)
- ENVIRONMENTAL CLEARANCE
- OTHER

**BORROWER & GUARANTOR
FINANCIAL ANALYSIS**

The credit officer should spread the applicant's financial statement to evaluate the strength of net worth and the adequacy of income.

Particular attention should be paid to the applicant's current position and the capability to generate cash to provide additional equity to the subject project.

INTEREST RESERVE ANALYSIS

INTEREST

An assumption must be made as to the average balance during the loan term. An assumption must also be made as to the average interest rate during the term.

These assumptions are very subjective, and therefore must be made on the basis of such matters as pre-sales of homes, which will determine how quickly loan funds will be taken down and how quickly they will be repaid as a result of the homes being delivered to the buyers. The interest rate assumption will be based on the historic behavior of rates and anticipated movement.

ILLUSTRATION:

Loan Amount \$500,000.

Assumed Average Balance x Assumed Interest Rate = Reserve
\$200,000. x 15% = \$30,000.

PROJECT ANALYSIS

Credit Officer must analyze the cost breakdown and make adjustments for interest reserve, etc. as necessary; then analyze the projected sales activity and cost of sales. Based on the analysis of these and other matters which impact the economics of the transaction, the Credit Officer must determine if the loan amount must be adjusted up or down, equity requirements from the borrower, release provisions for lots and homes.

CREDIT OFFICER SITE INSPECTION REPORT

1. Describe site:

2. Describe surrounding area:

3. Describe access (highways, public transport, etc.):

4. Distances: Major Employment Area:
 Schools:
 Hospitals:
 Shopping:

5. Is proposed project suitable for this location?

6. Adverse conditions:

7. General impressions and comments:

Credit Officer:

(date)

EXHIBIT G

**LETTER OF INSTRUCTION
TO APPRAISER**

RE:

(Project Name)

(Location)

Consider this letter a contract for your services to perform an appraisal of the subject project. Your assignment will require your analysis of the current value of the land and the market value of homes to be constructed thereon.

This appraisal is being requested by this Bank in connection with a construction loan application in the amount of \$_____. The proceeds of the proposed loan would be used to finance the purchase of land, make site improvement, and construct [#] homes.

Your written report of value is to be submitted to the Bank by [DATE] and in accordance with our agreement, your fee for services will be \$_____, to be payable as follows:

Information concerning the existing property can be determined from the Seller, _____, or its agent _____.

With this letter, we are providing you with the following:

- A legal description of the land;
- A complete cost breakdown;
- A complete set of architectural plans and specifications for the home models to be constructed;
- A site plan; and
- Projected sales prices for the homes.

Additional information relating to the development of this project can be obtained by contacting the undersigned, or the Developer, _____, or its agent, _____. Your report to the Bank should be submitted in three

written copies and contain at least the following information substantiating your estimate of value:

- Home address and location of property;
- The name of the appraiser with a list of professional qualifications and a list of clients;
- The approximate time during which this value is valid.

- Discussion of real estate tax information (assessment rate, assessed value, tax rate);
- Location information (neighborhood trends, zoning, transportation, adjoining property, construction in progress, planned development in the area, etc.)
- Site information (topography, shape, size, utilities, site improvements, access, etc.)
- Proposed improvements (exterior and interior design, size, construction methods, construction materials, appearance);
- Recent sales of land and homes in the area;
- Information to support the current valuation of the real estate;
- Computation of value and final value estimate; and
- The valuation process should include sales value, cost value, and income value analysis.

It is understood that your responsibility is to the Bank only, and your report is not to be used for any purpose other than with respect to the subject loan application.

EXHIBIT F

**LETTER OF INSTRUCTION
TO INSPECTING ENGINEER**

RE:

(Project Name)

(Location)

Consider this letter a contract for your services which comprise two types of assignments. Your services are being required by the Bank in connection with the underwriting of a \$_____ loan, the proceeds of which are to be used to finance improvements to the site and construction of [#] of homes.

Your initial assignment is to review the following, which are enclosed with this letter:

- Site development plans and specifications;
- Plans and specifications for all home models;
- Cost breakdowns for all site work and construction;
- Soil reports; and
- Contracts for contractors and major subcontractors.

Your written report indicating your opinion as to the adequacy and correctness of the above is to be submitted to the Bank by [Date]. In accordance with our understanding, your fee for these services will be \$_____, to be payable as follows:

Your report should indicate how you have verified the various costs and why you agree or disagree with the estimates. Any additional information you may require may be obtained from _____, the developer or _____, his architect, or _____, his contractor.

If the requested loan is approved, we will require you to make site inspections at least once a week for the purpose of inspecting work in process, confirming that it has been done in accordance with the final plans and specifications, which were signed by the Bank, Developer and Contractor and that work is in compliance with zoning and building ordinances.

We will also require that you review and approve all requests for payment presented to the Bank by the developer on behalf of the contractor. Your report to the Bank should include the following:

- Date of inspection;
 - Draw request number;
 - Identify work in progress for each house under construction;
 - Trades and number of tradesman working during your inspection;
 - Weather conditions;
 - Site appearance;
 - Confirmation that work is on schedule;
 - Supply representative pictures of the work in progress;
 - Your opinion that remaining work on each house can be completed with the remaining loan funds allocated to the particular house; and
- Review and make recommendations to Bank of proposed changes in plans and specifications.

It is understood that for this part of your assignment, you will be paid a fee of \$____ for each site inspection and a fee of \$____ for each draw inspection. Any additional assistance required from you will be paid for at your hourly rate of \$_____.

It is understood that you are exclusive agent of the Bank and your reports, opinions and comments are made entirely for the benefit of the Bank, and they are not to be regarded as representations to or for the benefit of anyone else.

SECTION III

Construction Loan Administration

TABLE OF CONTENTS

	PAGE
Preface	1
I. Loan Administration.....	2
II. Loan Commitment and Documentation.....	3
III. Legal Representation	3
IV. Loan Closing.....	3
V. Post-Closing.....	4
A. Establishing Files.....	4
B. Monitoring Critical Dates.....	5
VI. The Cost Breakdown and the Loan Budget	5
VII Disbursement of Loan Proceeds.....	5
A. Loan and Equity Funds.....	6
B. Progress Inspection	6
C. Retainage.....	7
D. Maintaining Budget Balance.....	7
E. Reallocating Budget Items.....	7
F. Adequacy of Loan Proceeds	7
G. Confirmation of Payments.....	8
H. Stored Materials.....	8

VIII.	Construction Inspector.....	9
IX.	Interest	10
X.	Loan Budget and Cost Control.....	11
XI.	Site Inspections and Meetings	12
XII.	Compliance to Terms and Conditions of Loan Documents.....	12
XIII.	Regulating Housing Starts.....	12
XIV.	Insurance and Taxes.....	12
XV.	Release of Homes from Loan	13
XVI.	Governmental Approvals	13
XVII.	Settlement Procedures.....	13
XVIII.	Environmental Issues	14
XIX.	Accounting.....	14
XX.	Disposing of Documents.....	15
XXI.	Loan Problems	15
	A. Actions Not To Be Taken.....	16
	B. Actions To Be Taken.....	17
	C. Meeting with Borrower	17
	D. Assessment of Situation.....	17
	E. Choose a Plan.....	18
	F. Damage Control	18
EXHIBITS:	[- Mortgage Fund Program Forms]	
	A. Loan Instruction Sheet	
	B. Loan Budget	

- C. Application for Payment -- Stage Draw
- D. Application for Payment -- Percentage of Completion
- E. Letter of Instruction to Inspecting Engineer
- E-1. _Letter of Instruction to Inspecting Engineer
- F. _Monthly Loan Status Statement
- G. _Statement of Construction Sub-Loan and Refinance
- H. _Disbursement Request Form
- I. _Disbursement Funding Form
- J. _Construction Disbursement Projection
- K. _Report of Payment and Rate Adjustment
- L. _Trial Balance

PREFACE

The financing of construction and land improvements are forms of real estate lending which require the application of highly specialized underwriting and administrative skills.

Since there is a high degree of risk associated with this activity, it is essential to keep such risk at a minimum by adhering to prudent Bank-approved underwriting standards and diligent administrative practices.

While policies and procedures will of necessity from time to time change, until such change occurs by official action, all loans must be originated and administered in accordance with existing regulations. Any warranted exceptions to these regulations must be approved by the Bank's management before an exception can be permitted.

I. LOAN ADMINISTRATION

The administering of construction loans is a key element in a successful construction lending program. No other type of loans made by a bank requires such day-to-day administration. Nor does any other loan require such active participation by the administrator in the many phases of the construction project. During the course of the loan, amendments to the documentation, changes in the loan budget due to increases or decreases in cost, changes in completion schedules and the constant monitoring of the construction must all be diligently carried out.

The loan administration process must be taken into consideration when the loan originator is negotiating and underwriting the loan. The administrator should be consulted and should assist the underwriter in structuring the loan in order to facilitate the administration process.

The officer originating the loan should consult with the loan administrator advising of the proposed loan and its situation and requesting guidance relative to any specific needs to properly administer the loan; in particular, would be such matters as the selection of a construction inspector, disbursement procedures, etc.

Copies of all underwriting memoranda should be provided to the administrative section, along with projected dates for the loan closing and the start of construction.

After the loan is approved, the loan approval should be provided to the administrator, together with a copy of the underwriter's worksheets.

Procedural Construction Lending Guide, June 1993
Section 7 Construction Loan Servicing Procedures

II. LOAN COMMITMENT AND DOCUMENTATION

Prior to issuance of the commitment it is recommended that the administrator have an opportunity to review, and, if appropriate, make suggestions to improve the letter. Since the legal documents will govern the activities of the administration of the loan, it is important that all documents be reviewed and approved by the loan administrator, who should make sure that all documents comply with the requirement of the Bank's credit policy and procedures.

Mortgage Fund Operations Manual, October 5,1993 ***Section 3.6.4 Commitment Letter***

III. LEGAL REPRESENTATION

All loan documents, opinions as to compliance to governmental and other regulatory requirements, should be prepared by either the Bank's legal staff or a Bank-approved lawyer who is knowledgeable in real estate, national and local governmental regulations and external and internal banking regulatory requirements.

During the term of the loan the administrator will interact with the Bank's legal representative on such matters as amendments to documents, request for opinions relating to any changes in loan terms, or assistance in dealing with problem borrowers. It is suggested that the loan administrator get to know the approved legal representatives well. Lawyers each have their own style expressed in the design of the documents they prepare and while each may generally conform to the Bank's requirements, it will be up to the loan administrator to be satisfied with the ultimate documents and therefore it is essential that administrators work effectively with legal representatives.

IV. LOAN CLOSING

The loan closing, at which time the borrower must sign all documents required by the Bank and also must provide any information or evidence of compliance with all requirements of the Bank, should be attended by the Bank's legal representative, the originating officers and the loan administrator.

The closing is often the first time the administrator will meet the borrower, and it is important to establish that the borrower is from this time on to deal with the administrator with regard to all matters pertaining to the subject loan.

The closing provides the administrator with the opportunity to review with the borrower the Bank's payment procedures as indicated in the loan documents and in particular the construction loan agreement.

V. POST-CLOSING

Any information not previously provided to the administrator by the loan originator or underwriter should be given at this time. After receiving all available information, the administrator should prepare a Loan Instruction Sheet [Exhibit A].

A. Establishing Files

It is recommended that the administrator set up two files. One titled, "Legal" for documents which should be retained in a locked, fire-proof container with access limited to only authorized personnel who can only access the file by signing a security register each time they go into the file.

In addition to the documents, the file should also contain document checklist indicating each document in the file and also indicate any documents not received. For documents not received there should be a current master list maintained by the administrator indicating the status of each unreceived document and the name of the party responsible for its collection, i.e. lawyer, administrator, borrower, etc. The safeguarding of the legal document file is of paramount importance in the loan administration process. The second file that should be set up is the "Working" file. The working file should be sectioned for each of the following:

- draw schedule
- request for draws
- inspection reports
- correspondence
- ledger sheets showing disbursements and receipts
- ledger sheet for accrued and paid interest
- special instructions
 - release provisions
 - maturity or expiration dates for:
 - insurance
 - bonds
 - guarantees
 - letters of credit

It is also advisable to make a copy of the Construction Loan Agreement which can be referred to rather than disturbing the "Legal" file.

B. Monitoring Critical Dates

In addition to the two files for each loan, it is recommended that a master monitoring system be established in the department. One person should be designated to follow maturity and expiration dates for the following:

- insurance
- bonds
- guarantees
- letters of credit
- documents not received
- current financial statements of borrower
- other date-sensitive materials

The person responsible for monitoring should review the system daily and advise the loan administrator at least 30 days prior to significant dates in order for the administrator to take appropriate action.

The Procedural Construction Lending Guide, June, 1993 ***Section 7 Construction Loan Servicing Procedures***

VI. THE COST BREAKDOWN AND THE LOAN BUDGET

At the time the loan is underwritten, the borrower will submit a cost breakdown which should be reviewed with the plans and specifications. The cost breakdown should be a detailed presentation listing the cost for each trade and each construction and non-construction item, and approved by the Bank's inspector. The loan underwriter will then structure a loan budget indicating the specific "hard" or direct construction items and the "soft" or non-construction items which will be paid from the proceeds of the loan.

[Exhibit B]

VII. DISBURSEMENT OF LOAN PROCEEDS

The Construction Loan Agreement will stipulate the method of payment for construction costs and non-construction cost as negotiated by the loan originator. One of two ways are typically used when funding construction costs for homes, either the "stage" method or the "percentage of completed work" basis. The stage method is predicated on each house being segregated into four to eight parts. As each stage is completed, as verified by the Bank's inspector, loan funds will be advanced to pay accordingly.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.3.2 Land Status and Costs
Section 3.3.7 Construction Costs

The percentage of completed work method will schedule payment to be made on a weekly or every two week period for work completed, as verified by the Bank's inspector.

The non-construction cost can be paid with either method upon confirmation of the expense being covered by the loan budget and confirming that the funds advanced are used for the purpose represented by the borrower.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.8 Sub-Project Construction and Implementation

A. Loan and Equity Funds

The loan budget, which is included in the Construction Loan Agreement, indicates the items and/or work to be paid from the loan proceeds. What is not paid from the loan must be paid by the borrower. The Construction Loan Agreement will also stipulate when and how the borrower is to contribute its equity. If the borrower's equity contribution or any part of it is to be injected after the loan closing, it is recommended that the required funds be held by the Bank in an escrow account until the designated time or circumstances occur and the funds are injected. The items of responsibility should not be changed without approval by the appropriate Bank management and approval of the Bank's legal representative.

The borrower should submit all requests for payment on a form which has been approved by the Bank. [Exhibit C]

Mortgage Fund Operations Manual, October 5, 1993
Section 3.8.2 Equity Invested First

B. Progress Inspections

The request for a loan advance should be given to the Bank's inspector, who should perform an inspection and confirm that the work for which payment is requested has been completed. If the inspector does not concur that the amount of work represented has been completed or that work is not satisfactory, the amount requested should be reduced accordingly and the borrower should immediately be

notified and advised as to why the draw amount has been reduced, and what action is required by the borrower to correct the situation.

Mortgage Fund Operations Manual, October 5,1993
Section 3.9 Supervision of Construction

C. Retainage

It is recommended that when disbursement procedures are being developed that a retainage of 10% be included. The provision that 10% be retained from each draw for each trade may provide some protection for the Bank in the event a contractor fails to perform satisfactorily or fails to complete the work. The accumulated retainages can be used to pay for the incomplete work or pay to correct poorly-completed work. The retainage should then be released within 15 days after the work is completed and approved by the Bank's inspector.

Mortgage Fund Operations Manual, October 5,1993
Section 3.7.3 Disbursement of Proceeds From the Bud Bank

D. Maintaining Budget Balance

Disbursements must be made only after approval by the inspector and confirmation by the administrator that the budget is in balance. The budget can get out of balance if the borrower requests payment in excess of amounts allocated for specific work in the budget. For example, if Framing cost increases because the builder had to pay more for lumber than projected. Even though the inspector may verify that the Framing is in place and the value is there, the budget would be out of balance if the administrator paid accordingly. In such an event, the borrower should advise the administrator of the necessity of making a change in the budget or the borrower should provide the additional funds required to pay for the Framing.

E. Reallocating Budget Items

If the borrower wants to reallocate budget items to cover the additional cost, then proof must be provided that there is an excess in other categories which can be allocated to Framing. Another solution would be taking from the contingency reserve in the budget. In any case the borrower is required to confer with and obtain the Bank's approval prior to incurring additional expense or submitting a request for payment.

F. Adequacy of Loan

At the time of each disbursement the administrator should receive assurance that the funds remaining to be disbursed for hard costs are in the inspector's opinion adequate. The inspector should also indicate if the work is being completed on schedule and in accordance with the plans and specifications approved by the Bank.

G. Confirmation of Payments

It is the responsibility of the administrator to be sure that loan proceeds are in fact being paid by the borrower and contractor to all sub-contractors, material suppliers, and other entitled to payments. It is recommended that the Bank follow the procedure of requiring all payees to acknowledge each payment and that evidence of all previous payments be obtained by the Bank before disbursing current request for payments.

Confirmation can be accomplished by having contractors, sub-contractors or material suppliers sign an acknowledgement when they receive a payment, or payment checks can be issued by the Bank to the borrower and the trade or material supplier and endorsement of the check will act as confirmation.

H. Stored Materials

It is advisable not to pay for materials not installed. If it is necessary to pay for stored materials, the Bank should require they be stored in a locked, fully-secured facility and the inspector should have a complete list of all such items and should continually confirm that all materials are accounted for.

VIII. CONSTRUCTION INSPECTORS

The Bank will rely heavily on the construction inspector, who will represent the Bank at the construction site. It is therefore suggested that the Bank employ a representative who possesses specific knowledge and experience with the type of construction which will be the subject of the assignment. The inspector must be a person with high integrity and an ability to communicate effectively with borrowers, contractors and the Bank.

The loan administrator should thoroughly investigate the inspector's background and experience. The inspector should be advised of the assignment in writing [Exhibit E] and be provided with the Bank's requirements for the progress reports.

In the event a project gets into trouble, the inspector may be of great assistance in managing the construction to get the project completed or assist the Bank in obtaining qualified contractors to complete the project.

In the selection of a construction inspector, it is suggested that the administrator draw on experience which exist in the Bank's Administrative Department. This department has engineers on staff who could be helpful in evaluating the credentials of inspectors.

A note of caution: the borrower will be paying for the cost of inspection services, but the inspector will be exclusively the agent of the Bank, and all inspection reports and any representations made by the inspector are entirely for the Bank's benefit. By approving work for payment, the inspector is not making representations to the borrower or any other party as to the quality of construction, adherence to plans and specifications or any other matter. The borrower must rely on its own agents, such as architect, contractor or its own inspector, for any assurances it may require.

Mortgage Fund Operations Manual, October 5,1993
Section 2.2.2.5 Monitoring the Progress of the Project
Section 3.4 Supervision of Construction

IX. INTEREST

Provision for interest payment can be made in one of the following manners:

- part of the loan proceeds
- paid as due by the borrower as equity contribution
- capitalized
- accrued

The first option requires the underwriter to estimate the probable interest expense based on the loan term, the average loan outstanding during the term, and an estimated interest rate during the loan term. The resulting amount is included in the loan budget as "interest reserve" and is disbursed monthly by transferring the appropriate charge for the preceding month or quarter from loans in process to the Bank's income.

The second option is operated by billing the borrower for the appropriate amount on a monthly or quarterly basis.

The third option adds interest to the principal of the loan and interest then is charged on interest since it becomes a part of the total loan amount and is collected when the loan is paid off.

The fourth option is a variation on the third option, but instead of increasing the loan balance, it accrues and is collected when the loan is paid off. From an income standpoint it is not as beneficial as option three:

All methods require diligence by the administrator to be sure that the income is timely received and credited.

With option one, the administrator must be alert to the adequacy of the reserve and if the reserve falls below a level with which the administrator feels comfortable, the borrower must either assume making interest payments as they come due or deposit an amount stipulated by the administrator to the reserve.

When interest is billed directly, a period of 15 days beyond the due date is usually provided and if payment is not received by the 15th day, a second notice is sent and a late charge is assessed.

The collection of interest, regardless of the manner which is used, is a paramount responsibility and the administrator must maintain adequate and correct records to assure that interest due is received by the Bank.

X. LOAN BUDGET AND COST CONTROL

As noted previously, the administrator must make sure the loan budget is always in balance. Expenses incurred by the borrower must be carefully monitored to be sure that costs do not vary from the cost breakdown submitted and approved by the Bank when the loan was underwritten. Costs can be reallocated using the procedures indicated previously.

The loan documents must contain the provision that if at any time " that the Bank in its sole judgment believes there are not sufficient funds remaining to be disbursed from the loan to complete the project, then the borrower can be required to deposit with the Bank the funds necessary in the Bank's opinion to cover the deficiency."

In every construction project, there are legitimate cost variances as a result of increases in materials, labor, change orders due to plan changes, etc. It is up to the administrator to confirm the legitimacy of such changes and to take the appropriate action to protect the Bank's position. Consequences of such changes include the possible affect on performance/completion bonds, insurance coverage, guarantees by third parties, and purchase contracts.

Mortgage Fund Operations Manual, October 5,1993

Section 3.3.1 Eligible Sub-Project Costs

Section 3.3.2 Land Status and Costs

Section 3.3.3 Costs Recovery and Sales Price

Section 3.3.7 Construction Costs

XI. SITE INSPECTION AND MEETINGS

In addition to the detailed inspection performed by the Bank's independent inspector, it is advisable for the administrator to visit the project periodically to have a first-hand knowledge of the construction status. It is also a good practice to attend periodic job meetings held by the borrower and contractor with the sub-contractors.

It is important for the administrators to be as knowledgeable about the loans under their jurisdiction as possible. This practice helps avoid unpleasant surprises and also enables the administrator to more capably keep the Bank's management advised of the quality of the loan portfolio.

XII. COMPLIANCE TO TERMS AND CONDITIONS OF LOAN DOCUMENTS

It is of the utmost importance that loans be administered in strict accordance with the terms and conditions established in the documents. Failure to do so can place the Bank in a position of losing control of the loan and subject it to possible loss. Auditors and/or regulators with good cause may rate as substandard loans which do not comply with the loan documents. Such action, of course, affects the Bank's financial condition.

XIII. REGULATING HOUSING STARTS

If the Bank is restricting construction to only a limited number of model or sample homes, and the remaining construction for those homes which have been sold, it is up to the administrator to monitor the process.

Administrators should only approve housing starts when a bona fide sales agreement has been given to the bank. A bona fide agreement is one which is accompanied by a commitment for a mortgage from a reputable lender, thereby indicating the borrower can pay for the house when it is completed.

XIV. INSURANCE AND TAXES

During the loan term, the administrator must make sure that the real estate is adequately insured and that the Bank is named as a loss payee. Taxes must be paid as they come due to avoid any liens pre-empting the Bank's mortgage.

XV. RELEASE OF HOMES FROM LOAN

When homes are completed and delivered to the buyer, the home must be released from the mortgage lien. When the loan is underwritten, release provisions are established, usually requiring that either 110% of the loan balance for the home or 90% of the net sales price be paid for the release. The fact that with either provision the amount for release is larger than the amount of the loan for the home is calculated to have the loan for the entire project repaid when 70-85% of the units are completed. This procedure reduces the amount of profit available during construction for the borrower, thereby maintaining incentives to complete the project. The provision also reduces the risk to the Bank from having to stay in the loan until the last unit is sold. Quite often the last units in a project are slow in selling and sometimes prices are reduced just to get them sold. Such a situation could be a problem for the Bank if the sale price is not adequate to repay the Bank's loan.

Mortgage Fund Operations Manual, October 5, 1993
Section 3.5.2 Repayment and Maximum Loan Term

XVI. GOVERNMENTAL APPROVALS

There are usually several approvals required from controlling authorities which must be obtained prior to, during and at completion of construction. The officer originating the loan and the bank's legal representative must determine prior to the commencement of the loan just what will be required, and when and who will be responsible for obtaining approvals. The loan documents should be specific as to all approvals and the administrator must review the documents and establish a procedure of monitoring to be sure that at all times the Bank is protected by having copies in its file of all current approvals. Disbursement of loan proceeds must not be made unless approvals are current.

XVII. SETTLEMENT PROCEDURES

The Bank's legal representatives should coordinate all processes necessary to accomplish the loan settlement. It will be the responsibility of the legal representative to set up a "loan closing checklist" indicating all conditions and documents which must be completed for the settlement. The legal representative should work closely with the officer originating the loan and the loan administrator.

XVIII. ENVIRONMENTAL ISSUES

During the time the loan is being underwritten the originating officer must ascertain any environmental conditions and regulations (see Exhibit H in Section II) which will affect the project. Issues must be resolved prior to the commencement of the loan and the administrator must be vigilant in making sure that if matters occur during construction which are environmentally sensitive, that they are immediately resolved. The Bank's inspectors can assist in monitoring conditions at the site and to alert the administrator of possible environmentally sensitive matters. Controlling authorities will usually serve notice of environmental issues to the borrower, but may not advise the Bank. Borrower must be cautioned that the Bank must be made aware of any issues and must be provided with a solution approved by authorities for resolving such issues.

XIX. ACCOUNTING

The administrator must set up and maintain ledgers for the following:

1. Loan ledger
2. Interest accrued and received
3. Fees received
 - commitment
 - late charges
 - legal
 - inspection
 - other
4. Fees paid
 - legal
 - inspection
 - other
5. Escrows
 - borrower equity deposits
 - deposits from home purchasers
 - insurance proceeds

The specific forms of ledgers will be determined by the Bank's Accounting Department.

XX. DISPOSING OF DOCUMENTS

When a loan is paid in full, the files should be cleared of documents which are to be returned to the borrower or other parties. Specifically the following must be done:

- Recorded documents should be forwarded to the appropriate authority with instructions that they be marked as satisfied on the official records. The documents properly noted or satisfied should be sent to the borrower.
- Insurance policies should be returned to the borrower with a notation on the policy that the Bank no longer has an interest in the policy.
- Guarantees should be marked cancelled and returned to the guarantors.
- Letters of Credit should also be released in accordance with the instruction of the borrower.

XXI. LOAN PROBLEMS

During the term of the loan it is not uncommon for problems to occur. Such problems may be minor, may not be the fault of the borrower, and may not pose any real risk to the Bank. Regardless of how small a problem may appear, it should be quickly addressed by the Bank to avoid escalating. Minor problems may signal more serious problems. Accordingly, the administrator should be alert, for example, to the following:

1. Early requests to reallocate costs
2. Early requests for repayments from contingency reserves
3. Payment requests for work not performed
4. Cost overruns
5. Construction delays
6. Inadequate number of workers on the job
7. Changes in building concept or plans
8. Non-payment to contractors and material suppliers
9. Slow sales of homes
10. Cancellations of sales contracts
11. Reduction by the builder of sales price
12. Filing of liens by sub-contractors
13. Non-payment of interest on time

If any of the preceding or other suspicious events occur, the administrator must exercise great care in proceeding. Before carrying out an investigation of the matter the administrator should immediately advise the department manager. If an investigation indicates that in fact a problem does exist, a plan of action must be devised which when carried out will not put the Bank's legal position in jeopardy. Depending on the circumstances and the severity of the problem it may be advisable to involve the Bank's legal representative.

When a loan gets into trouble, relations between the Bank and the borrower usually deteriorate rapidly and decisively. Each party will assume a defensive position. On determining that a significant problem exists which cannot be simply and immediately resolved, the Bank should proceed as follows:

Mortgage Fund Operations Manual, October 5,1993
Section 3.11 Default

A. Actions Not To Be Taken

1. Do not talk to or meet with borrower or its representatives until
 - a. legal representative for the Bank has been engaged and is prepared
 - b. Bank's legal remedies have ben analyzed
 - c. loan documents have been analyzed
 - d. third party (guarantors and other) liability to Bank have been evaluated
 - e. accounting records and correspondence and memo files have been analyzed
 - f. assessment of regulatory/tax/accounting implications to the Bank are considered
 - g. pre-workout agreement is executed by borrowers (this is not a workout or forbearance agreement)
2. Do not issue instructions to the contractors, suppliers, leasing or sales agents, employees of the borrower or become involved in any manner which could be construed as "owner" actions. Such activities increase possible lender liability claims. If the property has been abandoned you can take action to protect the collateral.
3. Do not disclose information about the borrower or its problems to third parties without the written consent of the borrower.

B. Actions To Be Taken

1. Issue a notice of default
2. Obtain an updated current value appraisal
3. Obtain an environmental audit
4. Perform an on-site inspection
5. If appropriate, secure and protect the property
6. Be sure property is adequately insured
7. Keep guarantors informed
8. Document all information relating to workout negotiations. Be careful of content. Have legal representative approve all file information and letters.
9. Purge existing files of any subjective or non-essential materials which could be detrimental to the Bank.
10. Keep Bank management fully informed of loan status (i.e. non-accrual or foreclosure).

C. Meeting With Borrower

1. Attendees should include Bank's legal representative and two Bank representatives.
2. A pre-workout agreement should be executed stating terms to be negotiated.
3. Review status of loan
 - a. Past -- how it got where it is
 - b. Present -- where it is
 - c. Future -- where Bank wants it to be
4. Possible workout options
5. Require current financial information of borrower, guarantors and property
6. Legal representative should confirm the results of meeting to borrower or its representative to assure that all parties are in agreement as to what took place.

D. Assessment of Situation

1. Analyze borrower's and guarantor's financial conditions
2. Review appraisal
3. In the case of construction, analyze sources and uses of funds to complete
4. Analyze market conditions
5. Again assess regulatory/tax/accounting implications to the Bank

E. Choose a Plan

1. Forbear with borrower and restructure loan
2. Take deed in lieu of foreclosure
3. Foreclose
4. Discount loan and allow note or property to be sold

F. Damage Control

1. Knowledge
2. Personnel
3. Quick Action

MANAGEMENT REPORTS

It will be a responsibility of the administrative section to maintain regular reports for management and to compile special reports as required. Examples of some reports are the following:

1. Commitments outstanding [Exhibit H]
2. Total amounts of loans advanced
3. Income received for the period (i.e. monthly, quarterly, annually)
4. Delinquent loans
5. Loans in foreclosure
6. Fees received
7. Fees paid
8. Repayment forecast by month [Exhibit I]
9. Current index rates. As these rates change each loan must be adjusted in accordance with terms of the loan.

Mortgage Fund Program Reports [Exhibits G-M]

EXHIBITS

EXHIBIT A

Loan No.: _____

LOAN INSTRUCTION SHEET

Project: _____ Administrator: _____

Borrower: _____ Telephone: _____

Mailing Address: _____

Date Closed: _____ Maturity Date: _____

Loan Amount: _____

Interest Rate: _____

Interest Collection: Charge loan Bill borrower
 Capitalize Accrue _____

Interest Period: Monthly Quarterly Other: _____

Method of Payment: Stop Number
 % completed Other: _____

Retainage: _____ %

Retainage to be released: _____

Payments to be issued to: Borrower
 Borrower and contractor
 Borrower and Subcontractor and Material Suppliers
 Other:

BANK AGENTS: _____

Appraiser: _____

Address: _____

Phone: _____

Inspecting Engineer: _____

Address: _____

Phone: _____

Legal Representative: _____

Address: _____

Phone: _____

BORROWER'S AGENTS: _____

Architect: _____

Address: _____

Phone: _____

Contractor: _____

Address: _____

Phone: _____

Legal Representative: _____

Address: _____

Phone: _____

Guarantor: _____

Address: _____

Phone: _____

FEES: _____

Application (non-refundable): \$ _____ Rec'd: _____

Commitment: \$ _____ Rec'd: _____

Appraisal: \$ _____ Rec'd: _____

Inspecting Engineer: \$ _____ Rec'd: _____

Legal: \$ _____ Rec'd: _____

Other: \$ _____ Rec'd: _____

Comments and Special Instructions: _____

EXHIBIT B

LOAN BUDGET

CATEGORY	PROJECT COST	EQUITY	LOAN
LAND	\$ _____	\$ _____	\$ _____
SITE IMPROVEMENTS	\$ _____	\$ _____	\$ _____
INTEREST	\$ _____	\$ _____	\$ _____
LOAN FEES	\$ _____	\$ _____	\$ _____
SOFT COSTS:	_____	_____	_____
LEGAL	\$ _____	\$ _____	\$ _____
INSURANCE	\$ _____	\$ _____	\$ _____
FEES	\$ _____	\$ _____	\$ _____
TAXES	\$ _____	\$ _____	\$ _____
HARD COSTS:	_____	_____	_____
[List of Construction Items]	\$ _____	\$ _____	\$ _____
	_____	_____	_____
CONTINGENCY	\$ _____	\$ _____	\$ _____
TOTAL	\$ _____	\$ _____	\$ _____

EXHIBIT C

Loan No.:

STAGE DRAW

APPLICATION FOR PAYMENT #:

DATE:

PROJECT #:

HOUSE #:

BORROWER:

In accordance with the stage draw schedule which is included as Exhibit [] in the Construction Loan Agreement for the subject, you are requested to disburse loan proceeds for Draw # .

- 1. All work for which payment is requested has been completed in accordance with the plans and specifications approved by the Bank.
- 2. The work has been completed on schedule.
- 3. All funds disbursed previously have been paid for previously-billed labor and materials.

Attached to this report are acknowledgments of payment for each of those paid with the proceeds of Draw #_____.

- 4. To the best of our knowledge, there are no Events of Default under the subject Construction Loan Agreement.

Approved:

Owner:

(Bank Inspector)

EXHIBIT E

LETTER OF INSTRUCTION TO INSPECTING ENGINEER

RE:

(Project Name)

(Location)

Consider this letter a contract for your services which comprise two types of assignments. Your services are being required by the Bank in connection with the underwriting of a \$_____ loan, the proceeds of which are to be used to finance improvements to the site and construction of [#] of homes.

Your initial assignment is to review the following, which are enclosed with this letter:

- Site development plans and specifications;
- Plans and specifications for all home models;
- Cost breakdowns for all site work and construction;
- Soil reports; and
- Contracts for contractors and major subcontractors.

Your written report indicating your opinion as to the adequacy and correctness of the above is to be submitted to the Bank by [Date]. In accordance with our understanding, your fee for these services will be \$_____, to be payable as follows:

Your report should indicate how you have verified the various costs and why you agree or disagree with the estimates. Any additional information you may require may be obtained from _____, the developer or _____, his architect, or _____, his contractor.

If the requested loan is approved, we will require you to make site inspections at least once a week for the purpose of inspecting work in process, confirming that it has been done in accordance with the final plans and specifications, which were signed by the Bank, Developer and Contractor and that work is in compliance with zoning and building ordinances.

We will also require that you review and approve all requests for payment presented to the Bank by the developer on behalf of the contractor. Your report to the Bank should include the following:

- Date of inspection;
 - Draw request number;
 - Identify work in progress for each house under construction;
 - Trades and number of tradesman working during your inspection;
 - Weather conditions;
 - Site appearance;
 - Confirmation that work is on schedule;
 - Supply representative pictures of the work in progress;
 - Your opinion that remaining work on each house can be completed with the remaining loan funds allocated to the particular house; and
- Review and make recommendations to Bank of proposed changes in plans and specifications.

It is understood that for this part of your assignment, you will be paid a fee of \$____ for each site inspection and a fee of \$____ for each draw inspection. Any additional assistance required from you will be paid for at your hourly rate of \$_____.

It is understood that you are exclusive agent of the Bank and your reports, opinions and comments are made entirely for the benefit of the Bank, and they are not to be regarded as representations to or for the benefit of anyone else.