March 16, 2016

Kathleen Zadareky
Deputy Assistant Secretary for Single Family Housing
U.S. Department of Housing and Urban Development
451 7th Street, S.W., Room 9282
Washington, D.C. 20410

RE: FHA Single-Family Housing Policy Handbook Clarifications

Dear Deputy Assistant Secretary Zadareky,

The Mortgage Bankers Association (MBA)[1] thanks the Department of Housing and Urban Development (HUD) for its efforts in developing a new comprehensive Federal Housing Administration (FHA) Single-Family Housing Policy Handbook (Handbook). As the single authoritative source for HUD's single-family policies, this resource has been beneficial for lenders to ensure compliance with FHA program guidelines.

As valuable as this Handbook is to lender compliance with FHA program guidelines, there are many outstanding policies that still require clarification for lenders to originate FHA loans with confidence. MBA has been working with a cross-section of diverse lenders to identify the most common questions. A list of these issues is attached. Though MBA appreciates the issuance of additional written guidance to create the most clear, concise, and consistent policies, MBA encourages open conversations between FHA and its participating lenders on the clarification of existing guidelines.

Clarity in Handbook guidelines is critical to ensure compliance and to preserve access to FHA mortgage credit. If provisions in the Handbook remain unclear, lenders will be forced to assess their ability to assume the risk of originating FHA loans that implicate these unclear provisions. MBA encourages HUD to implement a temporary "good faith" implementation and enforcement period of the policies in question. Similar to the Consumer Financial Protection Bureau's (CFPB) consideration of lenders' good faith efforts to comply with the new TILA RESPA Integrated Disclosure (TRID) rule, MBA urges HUD to take the same approach, by examining lender compliance through corrective and diagnostic supervision until clarified guidance is published. To facilitate helpful and productive conversations between lenders and FHA, MBA also requests a meeting with FHA to provide a status update on the current implementation of Handbook guidance and to discuss provisions that require additional clarity.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

MBA greatly appreciates the efforts HUD has already put into developing the Handbook. Should you have questions or wish to discuss any aspect of these comments further, please contact Tamara King, Vice President, Residential Policy and Member Engagement, at (202) 557-2758 or tking@mba.org; or Katherine Tung, Policy Advisor, Residential Policy and Member Engagement, at (202) 557-2870 or ktung@mba.org.

Sincerely,

Stephen A. O'Connor
Senior Vice President Public Policy and Industry Relations

Appendix

FHA Handbook Clarifications

These outstanding Handbook questions have been categorized into groups. These groups are prioritized by order of importance. (Questions in these categories are not prioritized but are sub-sorted by topic).

Lenders have voiced how helpful it would be to receive answers from the help desk that also include the question asked. This format is especially helpful when lenders are sending many questions over the same period of time, which can often result in confusion if responses are received for only a portion of the questions asked.

Credit:

1. II. A. 5. d. iii. Manual Underwriting of Credit and Debt. The section states: "The lack of traditional credit history or the Borrower's decision to not use credit may not be used as the sole basis for rejecting the mortgage application." Given this paragraph, can a borrower with absolutely no credit usage be approved for a mortgage? The new 4000.1 mentions requirements to meet nontraditional credit and states that if it does not meet this criteria it is considered insufficient, but there is nothing indicating requirements for borrowers who fall within the insufficient credit criteria. Are they eligible? Under what guidelines?

2. II. A. 4. b. iv. I. Revolving Charge Accounts (TOTAL). The section states:

    > (I) Revolving Charge Accounts (TOTAL)
    >
    > (1) A Revolving Charge Account refers to a credit arrangement that requires the Borrower to make periodic payments but does not require full repayment by a specified point of time.
    >
    > (2) The Mortgagee must include the monthly payment shown on the credit report for the Revolving Charge Account. Where the credit report does not include a monthly payment for the account, the Mortgagee must use the payment shown on the current account statement or 5 percent of the outstanding balance.

    If a borrower pays off a credit card balance in full, can any debt payment for the credit card be eliminated from the borrower qualifying ratios? If so, must the credit card be closed/cancelled to eliminate debt payment or is paying off the balance sufficient?

3. II. A. 4. b. iv. O. Business Debt in Borrower's Name (TOTAL). The handbook is silent on payment history. Does FHA require a 12 month payment history for debts paid by the business?

4. The handbook is silent on automobile leases. What guidance should a lender follow as far as excluding a payment from debt to income ratios in the event the lease is paid in full?

5. II. A. 1. a. i. C. Borrower Authorization for Verification Information <u>and</u> II. A. 4. b. i. General Credit Review Requirements (TOTAL). In multiple sections of the handbook, specifically in the above mentioned sections, there is a requirement for the verification of

a non-borrowing spouse's social security number (SSN). In cases where the non-borrowing spouse has no SSN, it is required that a credit report be pulled with a name, date of birth, and address. However, traditional credit reporting agencies don't have the capability to pull a credit report without an SSN. This requirement makes it difficult for a borrower who has a spouse that is a foreign national to obtain FHA financing. How should a lender satisfy this requirement when a non-borrowing spouse does not have an SSN?

6. The handbook is silent on whether a lender must check a non-borrowing spouse in CAIVRS. Is a lender required to check a non-borrowing spouse in CAIVRS?

7. The handbook is silent on Income Based Repayment (IBR). HUD published an IBR FAQ, but did not state how long the IBR has to continue to use the lower payment. Lenders have called both the Denver and Atlanta HOCs and have been told if the IBR is for less than 12 months, the "regular" payment must be used. How long do IBR payments or even graduated payments have to last in order to be able to use the IBR payment in the qualifying ratios?

8. II. A. 4. b. iv. G. Deferred Obligations (TOTAL). For student loans in deferment, are lenders required to use two percent of the balance or can they use the estimated monthly payment as provided by the student loan holder?

9. The handbook is silent on repossessions. How should lenders handle repossessions under the handbook?

10. The handbook is silent on short sales on a second lien. How should a lender consider a short sale on a second lien? Specifically, does it need to meet the waiting period? What if it was moved to charge-off because it was included in a bankruptcy?

11. II. A. 4. a. v. Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (TOTAL).
    a. Does a file need to be manually downgraded if a non-mortgage debt is discovered and not reported on credit report?
    b. If a mortgage is not reported on the credit report and that same property was included in a bankruptcy, does the loan need to be manually downgraded?

12. II. A. 4. a. v. Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (TOTAL). The handbook states that if the file contains information or documentation that cannot be entered or evaluated by TOTAL, or additional information not considered in the AUS recommendation, this will affect the overall insurability of the mortgage and the loan should be downgraded. Underwriters are denying loans because of the handbook requirement that states that a mortgage that is undisclosed, no matter how old, has to be downgraded to a manual underwrite. However, based on conversations with an underwriter in the Denver HOC regarding rejected loans due to the fact that mortgages were appearing on Loan Safe reports that were old, foreclosed, and no longer on the credit report, the HOC underwriter said that a loan that was foreclosed many years ago would not require a downgrade to a manual underwrite and that a manual downgrade would only be required if the foreclosure was within three years of FHA case number assignment. This policy is not clear in the handbook. How should lenders interpret this guidance? Can a lender still proceed with the AUS "accept"

as long as the foreclosure is over three years at the time of case assignment and not reporting on credit due to the statute of limitations?

13. II. A. 4. b. iii. K. Housing Obligations/Mortgage Payment History (TOTAL). Is mortgage history required on the subject property or on all mortgages on credit? Is the rule for streamlines different?

Income:

14. The handbook is silent on income from State legalized marijuana businesses. If a borrower is employed by a State legalized marijuana business is the borrower's income eligible for an FHA loan?

15. The handbook is silent on foreign income history. Is income history earned in a foreign country acceptable for an FHA loan?

16. The handbook is silent on CAFE plans. A CAFE plan is a type of employee benefit plan established in accordance with Section 125 of the Internal Revenue Code. Benefits provided under a CAFE plan are excluded from gross income by the employer. For FHA income purposes, can the amount paid by the employer under the CAFE plan be added back to the borrower's gross income?

17. II. A. 5. d. ix. F. 1. Residual Income. "Debts and obligations" have been omitted from the residual income calculation, however, debts and obligations must be subtracted from total effective income to calculate residual income. How should lenders count for debts and obligations under the new handbook?

18. II. A. 4. c. xii. A. 2. Disability Benefits (TOTAL). The handbook shows disability benefits income must have a three year continuance as measured from the date of mortgage application. Everything else in the manual that requires a three year continuance is counted from the case number assignment date. Why are disability benefits being treated differently?

19. II. A. 4. c. ix. Commission income (TOTAL). Handbook language requires the mortgagee to deduct the unreimbursed business expenses in all cases, regardless of the percentage of commission income which requires tax returns under all circumstances. There are two separate documentation requirements listed, one for less than 25%, and one for greater than 25%, however there is only one explanation for calculation requirements. This contradicts the documentation requirements for borrowers with less than 25% commission income. Do business expenses need to be deducted when commission income is less than 25%?

20. II. A. 4. c. xii. D. Mortgage Credit Certificate (MCC) (TOTAL). Will this credit be added back to the PITI or will it be applied to the income? Per the HLC's it's up to the lender to decide, but most MCC's are not subsidies directly to the lender. Therefore a lender would assume they would credit the tax credit amount to the income for qualification purposes.

Assets:

21. II. A. 4. d. iii. P. Sale of Real Property. The handbook states that net proceeds from the sale of a property owned by a borrower can be used as an acceptable source of funds, provided it was an arm's length sale.
    a. Is this applicable to an ex-spouse refinancing and buying a client out of their previous home? Would the client who is bought out be able to use those proceeds to purchase a new home?
    b. Is an arm's length transaction limited to family members? Do identity of interest scenarios apply as well?

22. II. A. 4. d. iii. A. Checking and Savings Accounts (TOTAL).
    a. For a joint bank statement held in a borrower's name when the joint account holder is a minor, is an access letter required to demonstrate full access to the funds from the minor?
    b. If the account is held by a borrower and also in the name of a trust, what documentation is needed to prove access to the funds in this case?

23. II. A. 4. b. iv. N. Private Savings Club (TOTAL). Can FHA provide clarity on what they expect a lender to verify to determine if a private savings club is legitimate? Do we need a state charter? Will FHA require any proof? What would they require in the binder?

24. II. A. 4. d. iii. N. Sale of Personal Property (TOTAL). Are funds from a loan secured by an automobile eligible? The previous handbook did not make the distinction between personal property assets and financial assets that the new handbook does. During one of the FHA Training calls regarding the new handbook it was clarified that loans against cars may not be used for MRI. Are automobiles now considered personal property?

25. II. A. 4. d. iii. G. Interested Party Contributions. How should lenders interpret the handbook guidelines regarding the itemization of seller contributions? Two varying interpretations are listed below:
    a. The first interpretation is that when the purchase contract identifies specific seller fees, those are allocated in the seller column and any remaining funds are "itemized" as a seller credit.
    b. The second interpretation is that seller funds should be "itemized" against the closing costs in the seller column. Therefore, there would only be a seller credit if all closing costs have already been allocated to seller funds and there is still money left over.

    Which interpretation is correct?

Property:

26. II. B. 3. g. iii. Plumbing System. Does the appraiser need to make a specific statement in the appraisal report that the FHA minimum required distance between well and septic system appears to be met?

27. The handbook is silent on the use of individual water purification systems. Is the use of individual water purification systems, if any, when water from either a well or public system is contaminated required and/or permitted? ML 92-18 permitted the use of an

individual purification system and there is still a Purification System rider to the model legal documents listed on the HUD website.

28. II. A. 1. b. iv. 3. Restrictions on Property Flipping. HOCs are telling lenders that FHA case numbers should not be obtained during the 90 day waiting period for property flipping and are informing lenders to cancel case numbers that are obtained prior to the 90 days. Can a lender obtain a case number prior to the 90 days provided the case will ultimately comply with the property flipping rules? In some instances a lender may not even know there is a flipping problem until after a case number is obtained.

29. II. A. 8. a. xviii. C. 1. C. Holdbacks. In the 4155.2 4.6.d Escrow of Funds for completion, there were six requirements listed to allow for the use of these funds. In the 4000.1 handbook three of those requirements are no longer listed, specifically, repairs being due to weather conditions, property being habitable, safe and essentially complete, and deferred work being completed within six months. Was this removal intentional?

30. II. A. 8. j. Construction to Permanent. FHA now states that if the borrower has not owned the land for six months at the time of case assignment, the land is not eligible for Build on your own land and must be treated as "construction to permanent" mortgage, however the construction to permanent financing detailed in the handbook is a one-time close. Why is this the only option? The previous 4155 handbook allowed for land that was owned less than six months, as long as acquisition cost was used instead of value.

31. II. A. 8. a. xiv. A. 1. Identity of Interest Certification. In a case where a borrower moved into a property with an "active" contract prior to tenancy, HUD has stated that since the contract was written before the borrowers moved into the property, they could receive maximum financing without having to be a tenant for six months. However, the handbook seems to indicate that borrowers must live in a property for six months and then re-execute a new sales contract. Which rule governs?

32. II. A. 8. o. vi. A. Maximum Mortgage Amounts. The guidance around the LTV limits for HUD REO sales is unclear. What maximum LTV is permitted for REO transactions that include a repair escrow or $100 down with repair escrow? HUD provides instructions on calculating the maximum mortgage amount but does not give a maximum LTV. Is this intentional? Also, can the UFMIP be financed in all cases where it previously could not be in certain cases?

33. II. A. 8. o. HUD Real Estate Owned Purchasing. HUD instructions for processing and underwriting HUD REO sales with repair escrows are unclear. HUD now requires the lender to establish the repair escrow amount for an REO sale using the appraiser's estimate of the repair costs, however, HUD is not requiring the amount of the repair escrow to be inserted in the sales contract; nor requiring that both HUD and the purchaser agree to the repair escrow amount or that the purchaser and HUD re-execute the contract with the amount of the escrow clearly shown on the sales contract. This leaves the lender with the task of revising the contract or modifying the loan documentation to show the specific amount of the repair escrow outside of the contract, even though the lender is not a party to the sales contract and cannot amend it in any way. How should REO sales be processed and underwritten with repair escrows, and how should the sales contract be written to reflect the escrow amount?

FHA Operations Related:

34. II. A. 4. d. iii. J. Secondary Financing (TOTAL). If there is secondary financing involving a State Housing Finance Agency and the lender advances the funds for the secondary financing at closing, must the secondary financing still be held by the government agency prior to endorsement? Mortgagee Letter 2013-14 required the secondary financing to be held by the government agency prior to endorsement, but the new handbook does not seem to have the same requirement.

35. I. A. 3. c. iv. 3. b. v. Conflicts of Interest. The handbook states "Employees are prohibited from having multiple roles in a single FHA-insured transaction. Employees are prohibited from having multiple sources of compensation, *either directly or indirectly*, from a single FHA-insured transaction." What does indirect compensation mean in situations where the loan originator is the <u>owner</u> of a real estate company and receives company profits from the real estate company's FHA transactions?

36. The handbook is silent on principal reductions to obtain FHA insurance. When can a lender make a principal reduction in order to obtain FHA insurance and is there any limit on the amount of the principal reduction that can be made?

37. II. A. 1. b. ii. B.1-2. Excluded Parties.
    c. There is no guidance on the validity period for a Sam/LDP check or expiration. Should these be checked within a certain time frame from closing- for example, within 30 days? At times files may not close for over 60 days to do various issues, mainly new construction, and the LDP/SAM check may have been completed early in the process.
    d. Does the lender have to complete the SAM check on employees (Loan Originator, Loan Processor, Loan Underwriter) on a loan level basis? This would mean lenders would be checking these individuals daily, sometimes more than once a day depending on the file workload in a large center. Is it acceptable for the Lender to do a bulk check of SAM/LDP on a regular basis (monthly/bi-monthly)?

38. The handbook is silent on unused borrower escrow funds. ML 2013-29 outlined the parameters in which unused borrower funds from an escrow account could be applied to an FHA to FHA insured refinance transaction, specifically referencing the allowance of usage of unused borrower funds for case numbers assigned on or after November 1, 2013. The ML has been superseded in whole by the 4000.1, however there is no guidance given in the handbook outlining the parameters of what is allowed. In absence of this guidance, a lender could potentially apply these guidelines to case numbers assigned prior to November 1, 2013. Are there any applicable parameters for applying unused borrower funds from an escrow account to an FHA insured refinance transaction? Does this mean that a lender and borrower can decide how to use and apply unused borrower escrow funds in an FHA to FHA refinance transaction provided the lender complies with all other written policies in the handbook on refinances?

Quality Control (QC):

39. V. A. 3. a. i. Loan File Selection. Is the timing for the final QC reporting to FHA 60 days from the close of month of the QC determination or 60 days from the selection of the loan for QC?

40. V. A. 3. d. i. Quality Control Reviews of Specialized Mortgage Programs. In the QC section there are rules for QC on the “specialized programs” such as EEM – can FHA confirm in the handbook that this is not a separate test for QC and that it can be combined with the standard QC?

General:

41. III. A. 1. f. ii. C. Prohibited Fees and Charges. On slide 40 of the HUD Handbook Training Module 6, it states a tax service fee can be paid by the borrower at loan origination. However, the handbook prohibits a tax service fee for servicing. Why is there an inconsistency?

42. II. A. 2. a. Maximum Mortgage Amounts. Deferred interest is not specifically addressed in the handbook. Can deferred interest be paid off as a rate and term refinance as part of the maximum mortgage amount or must it be treated as cash out?

43. There are still many FAQs posted that reference the 4155. If these no longer apply, they should be removed to avoid confusion with the new handbook guidance.