

**DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT****24 CFR Parts 203 and 221**

[Docket No. FR-3899-F-02]

RIN 2502-AG55

**Office of the Assistant Secretary for Housing—Federal Housing Commissioner; Single Family Mortgage Insurance Premium**

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

**ACTION:** Final rule.

**SUMMARY:** This rule makes final the proposed rule published by the Department on January 26, 1996, which proposed many benefits to the mortgage lenders that would reduce their servicing costs and the confusion generated by adjustments to the annual mortgage insurance premium (MIP) on cases not endorsed within the first six months after amortization. The rule changes the method of payment and the reconciliation schedule and clarifies the due date. It is expected that the changes will result in an increase in MIP income, thereby strengthening the FHA insurance fund. Also, costly reconciliation now done by HUD will be cut.

Specifically, the rule provides that the FHA Commissioner can accrue MIP from the beginning of amortization (as defined in 24 CFR 203.251) on all Section 530 (of the National Housing Act) loans and risk-based loans, no matter what time frame exists between the endorsement date and the beginning of amortization. It also amends the existing regulation by requiring that mortgagees pay the monthly installments as due on or before the 10th of the month, whether or not collected from the mortgagor. A new system is being developed (and expected to be operational by Summer 1997) which would produce a monthly notice of premiums due, and the reconciliation will be made monthly by the lender when the premium is paid. A new Single Family Premium Collection Subsystem-Periodic (SFPCS-P) is being developed (and expected to be operational by Summer 1997) which will produce a monthly notice of premiums due, and the reconciliation will be made monthly by the lender when the MIP is paid, thus eliminating the requirement for annual reconciliation.

**EFFECTIVE DATE:** August 19, 1996.

**FOR FURTHER INFORMATION CONTACT:** John L. Stahl, Acting Director, Office of

Mortgage Insurance Accounting and Servicing, Room 2108, Department of Housing and Urban Development, 451 7th Street, SW, Washington, DC 20410, telephone (202) 708-1046. For telephone communication, contact Anne Baird-Bridges, Single Family Insurance Operations Division, at (202) 708-2438. Hearing or speech-impaired individuals may call HUD's TTY number (202) 708-4594. These are not toll-free numbers.

**SUPPLEMENTARY INFORMATION:****Background**

Section 320 of the Housing and Community Development Act of 1980 (Pub.L. 96-399) amended Title V of the National Housing Act (the Act) (12 U.S.C. 1702 *et seq.*) to add a new section 530. Section 530 requires, with respect to insurance of mortgages under Title II of the Act, the payment of MIPs upon receipt from the borrower, except HUD may approve payment of such premiums within 24 months of such receipt if the financial institution or mortgagee pays interest to the insurance fund. On July 15, 1982, at 47 FR 30750, the Department published a final rule that implemented section 530 by requiring mortgagees to pay the MIP in installments due on or before the 10th day of the month following the month in which payments are due from the mortgagors. On June 23, 1983, at 48 FR 28794, the Department published a final rule which set forth the requirement that the borrower pay a single premium when the mortgage loan is closed, which represents the total premium obligation for the insured loan. This change applied to all new mortgages insured under the Mutual Mortgage Insurance Fund; therefore, after the change took effect, section 530 was limited to mortgages insured under the Special Risk and General Insurance Funds.

Section 530 loans include all FHA loans endorsed prior to September 30, 1983, and all FHA loans insured under the Special Risk and General Insurance Funds after September 1983. Lenders are required to remit annual MIP in 12 monthly payments totalling one-half of one percent of the average outstanding principal obligation of the mortgage.

The risk-based premium became effective on July 1, 1991, for all loans insured under the provisions of the Mutual Mortgage Insurance Fund, in accordance with the Omnibus Budget Reconciliation Act of 1990 (Pub.L. 101-508) and the National Affordable Housing Act of 1990 (Pub.L. 101-625). Sections 203.284 and 203.285 of title 24 of the Code of Federal Regulations were

promulgated to implement the provisions governing risk-based premiums (See 57 FR 15208, April 24, 1992, and 58 FR 40996, July 30, 1993). Risk-based premiums have two components: The up-front premium and the periodic premium. Periodic premiums on risk-based loans are collected over a set number of years, depending on the loan-to-value ratio of the mortgage. Premium payments are paid in twelve monthly installments totalling one-half of one percent of the remaining insured principal balance of the mortgage, minus any amounts included to finance up-front MIP. However, there is an exception under § 203.285 for any mortgage with a term of 15 years or less, which requires premium payments totalling one-fourth of one percent of the insured principal balance.

**This Rule**

On January 26, 1996, the Department published a proposed rule at 61 FR 2644. The public was afforded a 60-day comment period. No changes to the January 26, 1996 proposed rule are needed as a result of the comments. Therefore, this final rule adopts the proposed rule without change. Below is a discussion of the changes made by this rule.

This rule changes the method of payment and the reconciliation schedule and clarifies the due date. Specifically, the rule provides that the FHA Commissioner can accrue MIP from the beginning of amortization (as defined in 24 CFR 203.251) on all Section 530 and risk-based loans, no matter what time frame exists between the endorsement date and the beginning of amortization. It also amends the existing regulation by requiring that mortgagees pay the monthly installments as due on or before the 10th of the month, whether or not collected from the mortgagor.

The rule revises §§ 203.262, 203.264, and 203.265 to reflect the new policy on monthly payment of MIPs. The revised provisions also apply to risk-based premiums under §§ 203.284 and 203.285.

Sections 203.262 and 203.264 apply to the scheduled payments. Existing § 203.264 requires that "any portion of the periodic MIP received by the mortgagee from the mortgagor on or after September 1, 1982, shall be paid to the Commissioner on or before the tenth of the month following the month in which it was received," provided that the full annual MIP be paid by the tenth of the month following the anniversary date of amortization. At the initiation of

the Section 530 Program, mortgagees were offered two payment options:

a. *The Basic Monthly Payment Method.* According to this method, the lender remits on a monthly basis, on or before the tenth of each month, a payment equal to all Section 530 MIP amounts collected from mortgagors during the preceding month, plus any portion of annual MIP remaining due for the current anniversary month whether collected or not.

b. *Optional Monthly Payment Method.* According to this method, the lender remits a monthly payment equal to  $\frac{1}{12}$ th of the total of all annual Section 530 MIPs for all mortgages in the mortgagee's servicing portfolio for the month, plus any annual premiums remaining due, without regard to MIP amounts collected from mortgagors.

Most lenders opt to pay the premiums as due. HUD systems are set up to reconcile remittances of MIP, late charges, and interest based on payment of monthly premiums by the 10th of the month; exceptions must be manually processed. This rule eliminates the option to pay the premiums when collected.

The two provisions to be modified for Section 530 loans also apply to the periodic portion of risk-based loans. Mortgagees submitting risk-based monthly premiums have been following HUD's policy on adjustment of initial MIP depending on the date of endorsement, and have been given the option of paying monthly premiums (1) "as due" or (2) "as collected".

Section 530 and risk-based monthly premium payments will be due on the first of the month after the beginning of amortization (as defined in 24 CFR 203.251) and must be received on or before the tenth. Reconciliation between amounts expected by HUD and amounts remitted by the lender will be accomplished after the date of endorsement, when the insurance information has been fed into the FHA Single Family Insurance System. As soon as possible after endorsement, HUD will begin verifying that the lender has paid the required monthly premiums due at that time on each case, and will begin notifying the lender on a monthly basis of any discrepancies existing between expected, versus remitted, amounts. Until SFPCS-P is implemented, lenders will continue to reconcile risk-based monthly premiums at case level using MGIC Investor Services Corporation, and Section 530 monthly premiums at portfolio level based on the Advance Notice of Annual Premiums for Anniversary Due Date, which is being sent by HUD.

New §§ 203.262 and 203.264 authorize the FHA Commissioner to accrue annual premiums from the beginning of amortization (as defined in 24 CFR 203.251) on all Section 530 and risk-based loans, no matter what time frame exists between the endorsement date and the beginning of amortization. This rule also deletes § 203.263 which provides for an adjustment on the accrual date of the initial annual MIP depending on the date of endorsement of the loan. Section 203.268 is revised to provide that if the insurance contract is terminated, the lender will pay a portion of the MIP prorated from the beginning of amortization (as defined in 24 CFR 203.251) to the month in which the loan is terminated. The final monthly payment will be due on the first of the month following termination.

The changes made by this rule provide many benefits to the mortgage lenders that reduce their servicing costs and the confusion generated by adjustments to MIP on cases not endorsed within the first six months after amortization. The result expected is an increase in MIP income, thereby strengthening the FHA insurance fund. The changes cut down on the costly reconciliation now done by HUD. (The cost of reconciliation on Section 530 and monthly risk based premiums exceeded \$7.5 million in FY 1994.)

According to research completed on FY 1993 cases, approximately 7% of cases were not endorsed within the first six months of amortization. Currently some lenders escrow the premiums received from the homeowners on Section 530 and risk-based loans and remit the premiums to HUD at the beginning of amortization rather than when the case is endorsed for insurance. This has led to much confusion and variations in the computation of initial premiums due, because some contingencies cannot be foreseen at settlement; i.e., endorsement before the beginning of amortization. The revised regulation prevents confusion for those cases endorsed outside the six-month window by requiring lenders to follow the same guidelines for all cases needing periodic MIP.

MIP income is expected to increase by approximately \$15 million per year. This amount represents the reduction in premiums now taken by the lenders for both Section 530 loans and risk-based loans, when the loans are endorsed over six months from the beginning of amortization. Lenders should not receive a reduction in monthly MIP due because of late endorsement for the following reasons:

a. This is inconsistent with HUD's policy on one-time and up-front MIP.

These amounts are paid within 15 days of closing, and no reduction is given based on the date of endorsement. On risk based loans, § 203.284 requires payment of periodic MIP for a specific number of years, depending on the loan-to-value ratio. When the loan is endorsed after the six-month window, the period of time for which payments are due is being reduced.

b. Often the late endorsement results from late submission of the closing package by the lenders to the Field Office.

The new § 203.264 requires that payment of the periodic MIP be received from the mortgagee on or before the tenth day of the month following the month in which it was due from the mortgagor. For example, for a case closed in August and amortized in September, the initial premium is payable to HUD by the lender no later than October 10. Monthly reconciliation replaces annual reconciliation. Once SFPCS-P is implemented, monthly notices will reflect a breakdown by case number and by month of the cumulative amounts of monthly premium, late charge, and interest due.

The rule changes the method of payment, and the reconciliation schedule, and clarifies the due date. Payment of the periodic MIP by the lender is to be made monthly, regardless when collected. Upon implementation of SFPCS-P, a monthly notice from HUD will be sent and reconciliation will be made monthly by the lender when the MIP payment is paid, thus eliminating the requirement for annual reconciliation. MIP shall be due, and payable to the Commissioner, no later than the tenth day of the month.

Lenders will be informed that they are responsible for all loans in their portfolio for which monthly payments are due, even if they do not appear on the monthly notice. Because of servicing transfers, endorsement delays, and terminations, monthly notices may not reflect the current status of the lender's portfolio and may require reconciliation.

The current Single Family Monthly Collection System used for MIP collection is not set up to reconcile payments received under the "Payment as Received" option. The new SFPCS-P is not being set up to reconcile these payments either. The system enhancements necessary to accommodate this option would not be cost effective, and are not necessary, because most lenders have chosen the other option anyway.

It should be noted that § 203.284(f) "Applicability of Other Sections" does not include § 203.264 as applicable to

mortgages covered by § 203.284, although HUD has taken the position that this provision is properly applicable to mortgages with risk-based premiums. This rule re-inserts a reference to § 203.264 that was inadvertently deleted when that section was published as a final rule (See 57 FR 15209, April 24, 1992). The rule also inserts references to §§ 203.262 and 203.265 in lieu of the current §§ 203.284 (d) and (e) which are being deleted. Similar changes are made to § 203.285(c).

#### Public Comments

Comments were received from three commenters on the January 26, 1996 proposed rule: One housing development fund and two mortgage corporations. One of the mortgage corporations fully supports the proposed rule. Below is a listing of the comments presented from the other two commenters. After each comment is the Department's response.

**Comment:** There are terminology conflicts between the regulations and the HUD approved Deed of Trust, and clarification of the terms and the changes to the HUD approved forms are requested before the rule goes into effect.

**Response:** HUD Handbook 4165.1 REV-1 CHG. 3, Endorsement for Insurance for Home Mortgage Premiums (Single Family) dated November 30, 1995 contains new model mortgage and note forms which remove conflicting terminology. These changes became mandatory on June 1, 1996.

**Comment:** The reconciliation of the initial notice produced after the SFPCS-P is completed will most likely contain thousands of unmatched items for each lender. These will result from years of unreconciled service transfers, terminations, incorrect case numbers, and endorsement delays. Therefore, the commenter strongly urges the Department to conduct a preliminary audit to quantify the extent of the reconciliation required by both the lenders and HUD and then determine an approach and implementation date.

**Response:** Since SFPCS-P is being designed to capture MIP payments at case level, bills will contain detailed information to enable lenders to reconcile their portfolios each billing period. Unidentified cases will not be carried forward on SFPCS-P. HUD is working to resolve all unidentified cases separately.

**Comment:** There should be some standard established and required for the endorsement process. The commenter is concerned that the elimination of the financial penalty

could result in far more than seven percent of the cases taking more than six months to be endorsed, which could further complicate the ongoing reconciliation process.

**Response:** As long as a mortgage is submitted to HUD within 60 days of closing as required by 24 CFR 203.255(b), HUD is committed to proceeding within a reasonable time with its pre-endorsement review and subsequent endorsement if the mortgage is determined to be eligible for insurance. In nearly all cases that do not raise questions of eligibility, the Mortgage Insurance Certificate (MIC) should be issued long before the first half of the amortization year has expired. HUD policy to date has not permitted Field Offices to deliberately delay issuance of the MIC until the end of the first half of the amortization year. HUD's Processing Center in Denver is meeting our national goal by processing cases for endorsement in 10 days with a reject rate of six percent or under.

**Comment:** The examples for timing of remittances and final payments on terminations need clarification.

**Response:** To further clarify the example for the timing of remittance as set forth in the proposed rule, the example has been revised to read as follows: For a case closed in August with amortization beginning in September, the initial premium is payable to HUD by the lender no later than October 10.

For terminations, the final monthly payment would be due on the first of the month following termination and payable to HUD no later than the 10th of the month following termination. For example, if a case is terminated in August, the final monthly payment would be payable to HUD no later than September 10.

#### Other Matters

##### *Environmental Review*

A Finding of No Significant Impact with respect to the environment was made in accordance with the HUD regulation at 24 CFR part 50, which implements section 102(2) (C) of the National Environmental Policy Act of 1969, for the January 26, 1996 proposed rule. Since this final rule makes no changes to the proposed rule, the Finding of No Significant Impact for the proposed rule shall serve as the finding for the final rule. The Finding of No Significant Impact is available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk.

#### Regulatory Flexibility Act

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)) has reviewed and approved this rule, and in so doing certifies that this rule does not have a significant economic impact on a substantial number of small entities. A review of the universe of approved mortgagees indicates that only a small percentage of them have assets of less than \$10 million. These can be considered "small entities" for purposes of this regulation. The number of "small entities" affected, therefore, is not substantial. Further, HUD records indicate smaller companies hold relatively few insured mortgages, and they tend to concentrate their business in the conventional mortgage market. Thus, even for those "small entities" affected, the impact is expected to be relatively insignificant.

##### *Executive Order 12612, Federalism*

The General Counsel, as the Designated Official under section 6(a) of Executive order 12612, Federalism, has determined that the policies contained in this rule will not have substantial direct effects on states or their political subdivisions, or the relationship between the federal government and the states, or on the distribution of power and responsibilities among the various levels of government. As a result, the rule is not subject to review under the order.

##### *Executive Order 12606, The Family*

The General Counsel, as the Designated Official under Executive Order 12606, The Family, has determined that this rule does not have potential for significant impact on family formation, maintenance, and general well-being, and, thus, is not subject to review under the order. No significant change in existing HUD policies or programs would result from promulgation of this rule, as those policies and programs relate to family concerns.

#### List of Subjects

##### *24 CFR Part 203*

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

##### *24 CFR Part 221*

Low and moderate income housing, Mortgage insurance, Reporting and recordkeeping requirements.

**Catalog of Federal Domestic Assistance**

The Catalog of Federal Domestic Assistance number is 14.117.

Accordingly, the Department amends parts 203 and 221 of title 24 of the Code of Federal Regulations as follows:

**PART 203—SINGLE FAMILY MORTGAGE INSURANCE**

1. The authority citation for part 203 continues to read as follows:

Authority: 12 U.S.C. 1709, 1715b; 42 U.S.C. 3535(d). Subpart C also is issued under 12 U.S.C. 1715u.

2. Section 203.262 is revised to read as follows:

**§ 203.262 Due date of periodic MIP.**

The full initial and each annual MIP shall be due and payable to the Commissioner no later than the 10th day after the amortization anniversary date.

**§ 203.263 [Removed]**

3. Section 203.263 is removed.
4. Section 203.264 is revised to read as follows:

**§ 203.264 Payment of periodic MIP.**

The mortgagee shall pay each MIP in twelve equal monthly installments. Each monthly installment shall be due and payable to the Commissioner no later than the tenth day of each month, beginning in the month in which the mortgagor is required to make the first monthly mortgage payment or, if later, in September.

5. In § 203.265, paragraph (a) is revised to read as follows:

**§ 203.265 Mortgagee's late charge and interest.**

(a) Periodic MIP which are received by the Commissioner after the payment dates prescribed by §§ 203.262 and 203.264 shall include a late charge of four percent of the amount paid.

\* \* \* \* \*

6. Section 203.268 is amended by revising paragraph (a) to read as follows:

**§ 203.268 Pro rata payment of periodic MIP.**

(a) If the insurance contract is terminated before the due date of the initial MIP, the mortgagee shall pay a portion of the MIP prorated from the beginning of amortization, as defined in § 203.251, to the date of termination.

\* \* \* \* \*

7. Section 203.284 is amended by removing and reserving paragraphs (d) and (e) and revising paragraph (f) to read as follows:

**§ 203.284 Calculation of up-front and annual MIP on or after July 1, 1991.**

\* \* \* \* \*

(d) [Removed and reserved]

(e) [Removed and reserved]

(f) *Applicability of other sections.* The provisions of §§ 203.261, 203.262, 203.264, 203.265, 203.266, 203.267, 203.268, 203.269, 203.280, and 203.282 are applicable to mortgages subject to premiums under this section.

\* \* \* \* \*

8. Section 203.285 is amended by revising paragraph (c) to read as follows:

**§ 203.285 Fifteen-year mortgages: Calculation of up-front and annual MIP on or after December 26, 1992.**

\* \* \* \* \*

(c) *Applicability of certain provisions.* The provisions of §§ 203.261, 203.262, 203.264, 203.265, 203.266, 203.267, 203.268, 203.269, 203.280, 203.282, 203.284(c), and 203.284(g) are applicable to mortgages subject to premiums under this section.

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**PART 221—LOW COST AND MODERATE INCOME MORTGAGE INSURANCE**

9. The authority citation for part 221 is revised to read as follows:

Authority: 12 U.S.C. 1715b, 1715l; 42 U.S.C. 3535(d). Section 221.544(a)(3) is also issued under 12 U.S.C. 1707(a).

**§ 221.251 [Amended]**

10. Section 221.251(a) is amended by removing from the list “203.263 Adjustment of initial MIP.”

Dated: July 10, 1996.

Nicolas P. Retsinas,

*Assistant Secretary for Housing-Federal Housing Commissioner.*

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