

**DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT**
24 CFR Part 203
[Docket No. FR-4311-F-02]
RIN 2502-AH15
**Single Family Mortgage Insurance;
Electronic Underwriting**
AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Final rule.

SUMMARY: As part of Direct Endorsement processing of a single family mortgage for FHA insurance, FHA previously required a Direct Endorsement underwriter to review personally the appraisal report and credit application, including the analysis performed on the worksheets. HUD issued an interim rule in May 1998 to allow a Direct Endorsement lender to substitute an acceptable risk classification from a FHA-approved automated underwriting system (AUS) in lieu of a personal review by a Direct Endorsement underwriter. The interim rule is adopted without change as a final rule.

EFFECTIVE DATE: November 9, 2000.

FOR FURTHER INFORMATION CONTACT:

Vance Morris, Director, Office of Home Mortgage Insurance, Room 9266, Department Housing and Urban Development, 451 Seventh Street, SW, Washington, DC 20410, telephone (voice) (202) 708-2700. (This is not a toll-free number.) Hearing-impaired or speech-impaired individuals may access the voice telephone listed by calling the Federal Information Relay Service during working hours at 1-800-877-8339.

SUPPLEMENTARY INFORMATION:
Background

Until changed by an interim rule published on May 29, 1998 (63 FR 29506), the Direct Endorsement (DE) procedure required a DE underwriter to personally review the appraisal report and credit application, including the analysis performed on the worksheets, when a single family mortgage was processed for FHA insurance under the Direct Endorsement procedure. The DE underwriter would certify that the underwriter had personally reviewed the credit application and appraisal report on all mortgages originated under the DE procedure. With the introduction of automated underwriting systems, the need for human underwriters to review certain aspects of the mortgage loan application has been substantially diminished. The regulatory change

made by the interim rule allowed the lender to substitute an "accept" risk classification from a FHA-approved automated underwriting system in lieu of a personal review by a DE underwriter of the borrower's credit and capacity to repay the mortgage.

An automated underwriting system (AUS) performs an analysis of the loan application and provides risk grades or classifications as to the probability of mortgage default. The AUS either provides an acceptable risk classification (using such terms as "accept" or "approve") for the application based on information provided by the lender, or refers the application for further review by an individual underwriter. FHA controls the approval of all proprietary AUS's, determines the risk it is willing to accept (i.e., the score necessary to allow the loan to be considered an "accept" or an "approve"), and enters into agreements with the AUS vendors outlining what elements of the mortgage application it is permitting the AUS to evaluate. FHA, at its discretion, may determine that the AUS may be used to review elements of the applicant's credit and capacity.

FHA will continue to require a personal review for those mortgage applications referred to an individual underwriter and to require that the lender certify that all other aspects of the mortgage transaction, including data integrity and eligibility rules, meet FHA requirements. Further, the mortgage lender remains responsible for those aspects of the credit and capacity not evaluated by the AUS, including eligibility requirements, as well as the integrity of the data used by the AUS to arrive at the "accept" risk classification.

Public Comments

HUD received one comment on the interim rule from a DE underwriter.

Comment. The commenter stated that it would be prudent for HUD to retain a requirement for a qualified person to sign off on each loan. The commenter expressed concern that a person would need to ensure the integrity of information, such as that taken from a Builder's Certification for a new home, or make judgment calls concerning a need for repairs to a home. The same commenter expressed concern over what he characterized as "HUD's choice" of Freddie Mac's Loan Prospector, objecting to Freddie Mac's charge for access to that AUS system.

HUD Response. Under the rule as revised on May 28, 1998, the lender must still sign and submit to HUD, before the mortgage is endorsed for insurance, the Form HUD-92900-A that

holds the lender accountable for data integrity. The lender will have the option to decide who signs for the lender on the form certifying to the accuracy of the data used to determine the credit and capacity of the borrower, and may designate the DE underwriter for this purpose. The DE underwriter will still be responsible for review of the property, including repair requirements. An AUS will eliminate only the mandatory personal review of credit and capacity to repay, not the underlying collateral.

HUD did not approve Freddie Mac's licensing fees as part of the approval process, and does not expect to approve such fees for other systems. As other AUSs receive HUD approval, we expect that this will lead to market competition regarding fees for access to AUS processing for FHA-insured mortgages. Since the interim rule was published, HUD has approved Fannie Mae's Desktop Underwriter, as well as PMI Mortgage Services' pmiAURA, and is continuing to evaluate other systems.

HUD has concluded that no change to the interim rule is needed.

Findings and Certifications
Environmental Finding

A Finding of No Significant Impact with respect to the environment was made in accordance with HUD regulations at 24 CFR Part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969, at the time of the interim rule. The Finding of No Significant Impact remains available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of the General Counsel, Department of Housing and Urban Development, Room 10276, 451 Seventh Street, SW., Washington, DC 20410.

Federalism

Executive Order 13132 (entitled "Federalism") prohibits, to the extent practicable and permitted by law, an agency from promulgating a regulation that has federalism implications and either imposes substantial direct compliance costs on State and local governments and is not required by statute, or preempts State law, unless the relevant requirements of section 6 of the Executive Order are met. This final rule does not have federalism implications and does not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the Executive Order.

The Regulatory Flexibility Act

In accordance with 5 U.S.C. 605(b) (the Regulatory Flexibility Act), the Secretary by his approval of this rule hereby certifies that this rule does not have a significant economic impact on a substantial number of small entities because it allows mortgage lenders greater flexibility and reduces underwriting time and expense.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) (UMRA) requires Federal agencies to assess the effects of their regulatory

actions on State, local, and tribal governments and on the private sector. This final rule does not impose, within the meaning of the UMRA, any Federal mandates on any State, local, or, tribal governments or on the private sector.

List of Subjects in Part 203

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

Catalog of Federal Domestic Assistance

The Catalog of Federal Domestic Assistance number for this program is 14.117.

Accordingly, the amendment to 24 CFR 203.255(b)(5) made by interim rule published on May 29, 1998 at 63 FR 29506 is adopted as a final rule without change.

Dated: October 2, 2000.

William C. Apgar,

Assistant Secretary for Housing-Federal Housing Commissioner.

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