



OFFICE OF HOUSING

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

FEB 14 2020

RE: TRIBAL CONSULTATION ON HUD'S PROPOSED RULE ON MORTGAGE INSURANCE FOR TRANSACTIONS INVOLVING DOWNPAYMENT ASSISTANCE

Dear Tribal Leader:

HUD is developing a proposed rule to establish underwriting criteria that mortgagees must follow when underwriting a mortgage for FHA insurance that involves downpayment assistance provided by state, local, and Tribal governments.

This letter is to inform you about this rulemaking effort. In accordance with HUD's Government-to-Government Tribal Consultation Policy, HUD is seeking your feedback.

HUD will consider your comments in developing its proposed rule. Thereafter, you will be notified if a proposed rule is published in the Federal Register, and you will have another opportunity to comment through the public comment process.

Background:

The National Housing Act ("NHA") establishes criteria for single-family mortgages that are eligible for mortgage insurance provided by the Federal Housing Administration ("FHA"). One of the longstanding eligibility criteria is that the borrower must provide a minimum cash investment in the property, sometimes referred to as a downpayment. Specifically, section 203(b)(9)(A) of the NHA (12 U.S.C. 1709(b)(9)(A)) requires that for a mortgage to be eligible for FHA mortgage insurance, the borrower must have provided a Minimum Required Investment ("MRI") of 3.5 percent of the value of the property.

Under section 203(b)(9) of the NHA, the MRI may be provided from the borrower's pre-existing funds or a gift from an eligible source may be provided to the borrower to use for any portion of the MRI. In addition, a family member may lend the borrower all or a portion of the MRI. But if the family loan of the MRI is secured by a lien on the property, such lien must be subordinate to the FHA-insured mortgage, and the sum of any lien securing the repayment of the family loan and the insured mortgage will not exceed 100 percent of the appraised value of the property, plus any fees connected to the mortgage.

In 2008, the Housing and Economic Recovery Act ("HERA") amended section 203(b)(9) of the NHA to restrict the permissible sources of the borrower's MRI. The amendment added section 203(b)(9)(C) (12 U.S.C. 1709(b)(9)(C)), which provides that the MRI may not come from a "prohibited source" as defined by the NHA. Specifically, prohibited sources are:

1. The seller or any other person or entity that financially benefits from the transaction.
2. Any third party or entity that is reimbursed, directly or indirectly, by any of the parties described in clause 1.

HUD has in the past sought to clarify the MRI downpayment requirements in accordance with the statutory restrictions. In 2008, FHA issued a Mortgagee Letter providing notice of HERA's MRI restrictions.¹ In 2012, HUD issued an interpretive rule, which viewed section 203(b)(9)(C) as not prohibiting FHA from insuring mortgages originated as part of the homeownership programs of federal, state, or local governments or their agencies or instrumentalities when such entities are also providing assistance for the borrower's MRI, referred to as downpayment assistance ("DPA").² In 2013, FHA published a Mortgagee Letter to provide documentation requirements for such DPA.³ The 2013 Mortgagee Letter noted that "[a]ll other requirements applicable to secondary financing transactions remain in full effect, including the requirement that such financing comply with the prohibited source provisions if such financing will be providing the borrower's required Minimum Cash Investment." However, FHA continues to have concerns that lenders are originating mortgages for FHA insurance with downpayment assistance that does not comply with the statute.

Proposed Rulemaking and Tribal Feedback:

HUD intends to propose revisions in its regulations for FHA insurance of lenders of single-family mortgages to address these continuing issues by:

1. Ensuring that lenders who originate mortgages for FHA insurance that involve DPA are complying with section 203(b)(9) of the NHA in its entirety, including the provisions that prohibit the use of funds provided by a person or entity that financially benefits from the transaction to satisfy the borrower's MRI;
2. Providing criteria by which lenders originating a mortgage for FHA insurance can confirm that the downpayment assistance provided on a given mortgage is not from a prohibited source because the provider entity is not receiving a financial benefit that would render such assistance to be prohibited under NHA section 203(b)(9)(C);
3. Proposing that a de minimis administrative cost over the amount of the assistance would not constitute a financial benefit prohibited under section 203(b)(9)(C);
4. Clarifying the allowance of gift contributions, and contributions from family members that meet statutory requirements; and
5. Defining both "financially benefits" and "de minimis administrative costs" for the benefit of a lender's determination whether the source of any potential downpayment assistance

¹ HUD Mortgagee Letter 2008-23 superseded as incorporated into HUD Handbook 4000.1.

² See Interpretive Rule, 77 FR 72219.

³ HUD Mortgagee Letter 2013-14 superseded as incorporated into HUD Handbook 4000.1.

is prohibited under section 203(b)(9)(C).

In addition to accepting general public comments, HUD has specific questions for comment. We anticipate asking questions on:

1. What is a reasonable amount per transaction for de minimis administrative costs of providing DPA? By what means should HUD establish the amount for administrative costs?

2. Would a definition of “transaction” as the purchase of the real property, together with the mortgage financing of the purchase that is insured (or to be insured) by HUD and the MRI funding (through e.g., DPA) required for the purchase-mortgage financing, adequately encompass all the ways in which a DPA provider could generate funds from providing the borrower’s MRI on an FHA-insured mortgage?

3. Should HUD require that a lender wishing to originate a mortgage for FHA insurance that uses DPA ensure that the governmental entity providing the DPA is not a prohibited source by having access to the provider’s DPA funding plan showing all sources of funds and an accounting of all associated costs? Should any other items be required as part of such a funding plan?

4. Should HUD require lenders to submit any agreements with a DPA provider, and sample agreements between the borrower and the DPA provider, regarding use of the DPA to originate a mortgage for FHA insurance? What changes or revisions to any such agreement should cause HUD to require the lender to resubmit the operative agreements to ensure against a prohibited financial benefit?


5. Should HUD require lenders to ensure that DPA provided by a governmental entity is being provided in respect to property over which it exercises governmental authority (or, in the case of Federally Recognized Indian Tribes, also in respect to borrowers who are enrolled members of the tribe)?

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Given our government-to-government relationship, we are seeking your views as a tribal leader on items that should be included as we develop these policy proposals. You may submit your comments to HUD within 30 days of the date of this letter by e-mail to HUDRegsTribalConsult@hud.gov.

Thank you for your continued interest and support of the Department's programs.

Sincerely,



John L. Garvin
General Deputy Assistant Secretary for
Housing

cc: Executive Director, Tribally Designated Housing Entity