



Housing Policy Council
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June 18, 2021

Lopa Kolluri
Principal Deputy Assistant Secretary, Federal Housing Administration (FHA)
US Department of Housing and Urban Development (HUD)
451 7th Street, SW
Washington, DC 20410

Dear Ms. Kolluri:

Thank you for your engagement with the housing finance industry on issues related to FHA's COVID-19 loss mitigation programs and for contacting the Housing Policy Council (HPC)¹ for an introductory policy discussion on a wide range of issues. During that policy conversation, we mentioned our concerns with implementation of the FHA 4000.1 Handbook updates by the August 17, 2021 effective date *and* highlighted one topic of particular concern, the new requirement for servicers to self-curtail claims for property preservation expenses if specific benchmark timelines are missed. We expressed that we do not believe FHA has the regulatory authority to institute this significant policy change and that we planned to submit a letter to you explaining our position.

Therefore, we are following up with this letter, to present a summary of the problematic Handbook change at issue and, more importantly, our rationale for questioning FHA's authority to pursue this change administratively, rather than regulatorily. We ask that FHA remove this policy change in advance of the August 17, 2021 effective date or any future effective date, should FHA postpone implementation of the Handbook.

The specific Handbook change of concern is located Section III.A.2.t.i.(E), page 754 of the Handbook 4000.1 PDF document dated April 19, 2021. The text indicates that the servicer is obligated to "self-curtail" property expenses if any of a handful of deadlines are missed. In other words, the Handbook states that the servicer is expected to reduce the total claim amount filed if timelines are missed, which transfers the payment for property protection and preservation costs that were previously eligible for reimbursement from FHA to the servicers.

¹ The Housing Policy Council is a trade association comprised of the leading national mortgage lenders and servicers, mortgage and title insurers, and technology and data companies. HPC advocates for the mortgage and housing marketplace interests of its members in legislative, regulatory, and judicial forums. Our interest is in the safety and soundness of the housing finance system, the equitable and consistent regulatory treatment of all market participants, and the promotion of lending practices that create sustainable homeownership opportunities in support of vibrant communities and long-term wealth-building for families. For more information, visit www.housingpolicycouncil.org.

This significant new cost to servicers is neither authorized nor required under the existing regulations.

The updated Handbook language that we are referencing reads as follows:

(E) Curtailment of Claims

Mortgagees are responsible for self-curtailment of interest and property expenses on Single Family claims when the Initiating Foreclosure Time Frame, Notice of Foreclosure Time Frame, Reasonable Diligence Time Frame, Conveyance to HUD Time Frame, or reporting requirements are not met. Property expenses do not include real estate taxes and hazard insurance premiums.

For each of these self-curtailment time frames, the time frame begins on the **earlier** of the date the action should have been taken in accordance with HUD requirements or the actual date the action was taken.

The curtailment of property expenses *is* addressed in the regulation but is only authorized when a mortgagee misses the conveyance timeline. In contrast, the Handbook update includes the expanded list of critical timelines with which the servicer must comply to receive full reimbursement. This change is not consistent with the requirements set forth in the relevant section of the code of federal regulations. The specific regulation, 24 CFR 203.402(g)(2), which cross references 24 CFR 203.359 (cited in the Handbook using the term, “conveyance timeframe”²), provides that “insurance benefits paid in connection with foreclosed properties ... **shall include**” (emphasis added) protection and preservation expenses incurred before the conveyance deadline:

Section 203.402(g)(2)

*(2) For mortgages insured under firm commitments issued on or after November 19, 1992, or under direct endorsement processing where the credit worksheet was signed by the mortgagee's underwriter on or after November 19, 1992, reasonable payments made by the mortgagee, with the approval of the Secretary, for the purpose of protecting, operating, or preserving the property, or removing debris from the property **prior to the time of conveyance required by §203.359 of this part.***

Section 203.359

(b) For mortgages insured under firm commitments issued on or after November 19, 1992, or under direct endorsement processing where the credit worksheet was signed by the mortgagee's underwriter on or after November 19, 1992 – (1) Conveyance by the mortgagee. The mortgagee must acquire good marketable title and transfer the

² HUD Handbook 4000.1 III.A.2.t.i. In addition, the Department requires properties to be in “acceptable conveyance condition,” which requires mortgagees to ensure that the property is undamaged, secured/winterized, free from vandalism, has good and marketable title, and is in broom-swept condition. See id. III.A.2.t.ii.(A).

property to the Secretary within 30 days of the later of: (i) Filing for record the foreclosure deed; (ii) Recording date of deed in lieu of foreclosure; (iii) Acquiring possession of the property; (iv) Expiration of the redemption period; or (v) Such further time as the Secretary may approve in writing.³

As you can see, the relevant regulatory text related to property preservation expenses does not allow for the foreclosure commencement or reasonable diligence timeframes as a limiting factor on the reimbursable fees authorized by Section 203.402(g)(2). Section 203.402(g)(2) only references the conveyance timeline in Section 203.359 as a limitation on property preservation expenses to be included in an FHA insurance claim—it does not reference the regulations providing timeframes for foreclosure initiation (Section 203.355(a))⁴ or reasonable diligence (Section 203.356(b)).⁵ Moreover, this distinction is reinforced by the text of Section 203.402(k) regarding debenture interest in FHA claims, where FHA explicitly included multiple deadlines as limiting factors to authorized interest including, among others, the foreclosure commencement, reasonable diligence, and conveyance timeframes.

Because the plain language of the regulation does not reference the foreclosure commencement or reasonable diligence timeframes—to the contrary, it states that property preservation expenses predating the conveyance deadline “shall” be reimbursed—HUD does not have the regulatory authority to curtail claims for property preservation expenses based on a missed foreclosure commencement or reasonable diligence timeframe. Had the intent of the regulation been to prohibit servicers from claiming for such expenses, section 402(g)(2) would have referenced sections 355(a) and 356(b) in the way that it referenced section 359. FHA’s regulatory decision not to include sections 355(a) and 356(b) as limitations on reimbursement means the regulation requires that FHA “shall” reimburse property preservation expenses as long as the mortgagee meets the conveyance deadline in section 359.

Our concerns with the legal underpinning for this Handbook change are further substantiated by the activities of FHA and the HUD Office of Inspector General in 2015 and 2016, when the Department initiated a rulemaking effort that was subsequently abandoned. That 2015 Proposed Rule⁶ included potential changes that were *similar* to those that would take effect under this Handbook update, changes that were strongly opposed by industry, as evidenced by comments submitted at that time. The rulemaking exercise is a clear indication that HUD was aware that a modification to the regulation was required to execute any limitations on property expense reimbursements for failure to meet the full set of timeframes included in the listing in this new update to the Handbook. The subsequent HUD-OIG report⁷

³ *Id.* § 203.359(b) (emphasis in original); *see also* HUD Handbook 4000.1 (effective Jan. 2, 2020), § III(A)(2)(t)(i).

⁴ Section 203.355(a) provides that the general timeline for the mortgagee to “commence foreclosure” is “within six months of the date of default or within such additional time approved by HUD”.

⁵ Section 203.356(b) provides the regulatory authority for establishing the “time frame that is determined by the Secretary to constitute ‘reasonable diligence’ for each State...”

⁶ **Federal Register** /Vol. 80, No. 128 /Monday, July 6, 2015

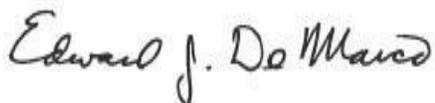
⁷ HUD OIG Audit Report 2017-KC-0001, “Single-Family Mortgage Insurance Claims,” October 14, 2016.

further affirms this point, because it also recommends that HUD reactivate its pursuit of a regulatory change to expand the FHA's legal authority to curtail property expenses for a broader array of missed timelines.

We believe that reimbursement for expenses related to the protection and preservation of properties that secure FHA mortgages is critically important for FHA, servicers, and communities. The servicer initiates a wide variety of preservation activities and covers the costs for these services on behalf of FHA, to protect the lien interest of the FHA, and this arrangement warrants reimbursement, as permitted under the terms of the current regulation. Given the clear limitations on FHA's regulatory authority to curtail these critical expenses for missed timelines, we respectfully request that FHA correct this error as quickly as possible, certainly before the updated guidance takes effect.

We appreciate your attention to this critical issue and would appreciate quick action to address what may be an unintentional error, given the broad array of updates that were included in this latest version of Handbook 4000.1. We do intend to submit a more extensive set of comments on the Handbook changes, jointly with the Mortgage Bankers Association, but felt that the property preservation issue was of such consequence that we wanted to address it separately. Should you have any questions or have an interest in additional discussion on this matter, please contact our EVP, Meg Burns, at 202-589-1926.

Yours truly,

A handwritten signature in black ink that reads "Edward J. DeMarco". The signature is written in a cursive, slightly slanted style.

Edward J. DeMarco
President
Housing Policy Council