



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

OFFICE OF THE ASSISTANT SECRETARY
FOR HOUSING-FEDERAL HOUSING COMMISSIONER

November 20, 2003

MORTGAGEE LETTER 2003-19

TO: ALL APPROVED MORTGAGEES

ATTENTION: Single Family Servicing Managers

SUBJECT: Partial Claims: Program Changes and Updates

The purpose of this Mortgagee Letter is to remind mortgagees of the proper use of the partial claim as a loss mitigation tool for defaulted FHA mortgagors, and to introduce several changes in the partial claim program which include:

- a reminder that mortgagees shall lose the incentive payment when loss mitigation claims are not submitted within 60 days of the date the partial claim subordinate lien is executed, or where the partial claim security documents are not forwarded timely,
- a **“One-Time Amnesty”** which is being provided to accept all outstanding partial claim related legal documents without penalty;
- additional guidance for calculating pre-foreclosure sale ratios where a partial claim had been provided to the mortgagor in a previous default.

This Mortgagee Letter supersedes the portion of Mortgagee Letter (ML) 2000-05 that addresses partial claims, starting on page 24 through page 29. The other loss mitigation provisions within ML 2000-05 were left intact. Several additional sections have been provided to clarify time frame and address document delivery issues.

Definition and Existing Guidance

Under the partial claim option, a mortgagee will advance funds on behalf of a mortgagor in an amount necessary to reinstate a delinquent loan (not to exceed the equivalent of 12 months worth of principal, interest, taxes, and insurance (PITI)). The mortgagor, upon acceptance of the advance, will execute a promissory note and subordinate mortgage payable to HUD. Currently, these promissory or “partial claim” notes carry no interest and are not due and payable until the mortgagor either pays off the first mortgage or no longer owns the property.

Following reinstatement, the mortgagee will file a partial claim for the amount of the advance plus the mortgagee's incentive fee, and forward a copy of the recorded documents to HUD. A contractor retained by HUD will service the partial claim notes.

HUD approval is not required in order for mortgagees to advance funds and file a partial claim, as long as the requirements detailed in this section are satisfied. This option provides mortgagees with a powerful tool to assist mortgagors threatened with foreclosure. However, this loss mitigation option should be used only if the mortgagee is confident that:

- The mortgagor has the long-term financial stability to support the mortgage debt; and,
- The mortgagor does not have the ability to repay the arrearage through a special forbearance or modification.

A. Loan Default

The loan must be at least four (4) payments due and unpaid, but may not be more than 12 months due and unpaid at the time the partial claim note is executed. The loan may not be in foreclosure when the partial claim note is executed. However, a mortgagee may remove a loan from foreclosure if the mortgagor's financial situation has improved sufficiently to justify a partial claim.

B. Mortgagor Qualifications

Partial claims may be offered to mortgagors who satisfy all of the following requirements:

- Have overcome the cause of the default;
- Have sufficient income to resume monthly mortgage payments;
- Do not have sufficient surplus income to repay the arrearage through a repayment plan;
- A mortgage modification is not appropriate;
- The mortgagor is an owner-occupant(s) committed to continuing occupancy of the property as a primary residence. A partial claim may not be used to reinstate a loan prior to a sale or assumption.

A mortgagee may consider a mortgagor who has filed a petition in Bankruptcy Court under Chapter 13 for a partial claim, only after obtaining the approval of the Bankruptcy Court. If the mortgagor has filed a bankruptcy petition under Chapter 7, the mortgagee must obtain Bankruptcy Court approval. In addition, the mortgagor must reaffirm the debt.

C. Property Condition

While the partial claim option does not include a loan-to-value restriction and no appraisal or broker's price opinion is required, the mortgagee must conduct a review sufficient to verify for FHA that the property has no physical condition(s) which adversely impact the mortgagor's continued use or ability to support the debt.

A mortgagor may not be able to support payments under a partial claim if the property is in such a deteriorated condition that repairs drain the mortgagor's monthly resources. An analysis of the mortgagor's surplus income should consider anticipated property maintenance expenses. If the mortgagee's inspection identifies a property in extremely poor physical condition, a partial claim may not offer a permanent resolution to the default.

D. Financial Analysis

The mortgagee is required to assess the mortgagor's financial status as described in Section H, page 10, of ML 00-05. HUD expects the mortgagee to project the mortgagor's surplus monthly income for a minimum of three months, and calculate the surplus income percentage.

If the financial analysis determines that the mortgagor does not have the ability to support the normal monthly payment, the partial claim option may not be used. In no case may a partial claim be used if the mortgagor's surplus income percentage is 0% or less than 0%. If the mortgagor has low surplus income (< 5%), mortgagees are encouraged to combine a partial claim with a special forbearance plan allowing the mortgagor to demonstrate the ability to make regular payments for a period of three (3) or more months prior to origination of the partial claim note.

Mortgagees must use good business judgment to determine if the mortgagor has the adequate surplus income to repay the arrearage through a special forbearance or mortgage modification before approving a partial claim. Mortgagees are encouraged to require mortgagors to contribute all available funds toward paying down the default, thereby reducing the amount of the partial claim debt. The lender must retain the financial analysis and supporting documentation in the claim review file that supports the decision that a partial claim was the appropriate loss mitigation option.

E. Combining Options

A partial claim may be utilized as a stand-alone tool, or incorporated as part of a special forbearance agreement. For example, if a mortgagor needs time to resolve the default, but will eventually be able to support the normal monthly payment but no more than that, a repayment plan or special forbearance may culminate in a partial claim. An existing repayment plan or special forbearance may also be converted to partial claim if the mortgagor's circumstances change. A partial claim may not be used in conjunction with a mortgage modification.

On August 29, 2002, the Department published Mortgage Letter (ML) 2002-17, **Special Forbearance: Program Changes and Updates** which provided new guidance for a Type II Special Forbearance. The Type II Special Forbearance combines a short-term special forbearance plan and a modification or partial claim as a single loss mitigation plan. It is an appropriate loss mitigation tool to utilize when there is any concern about the mortgagor's ability or commitment to keep the payments current following reinstatement. For more information on this related issue, please refer to ML 2002-17.

F. Allowable Provisions

The following provisions apply to all partial claim notes:

- The partial claim must fully reinstate the loan;
- The partial claim advance may include only principal, interest and escrow advances required to reinstate the loan;
- In no event may the total arrearage exceed the equivalent of 12 months PITI. The maximum partial claim advance for an Adjustable Rate Mortgage (ARM), Graduated Payment Mortgage (GPM), and Growing Equity Mortgage (GEM) loans is calculated by adding the specific PITI requirement for each of the monthly installments to be included in the partial claim.

The mortgagee may not include late fees, legal fees or other administrative expenses in the partial claim note. However, mortgagees may only collect legal costs and fees resulting from a canceled foreclosure action directly from the mortgagor to the extent not reimbursed by HUD and in accordance with HUD limitations. These requirements are provided in Chapter 4 of Handbook 4330.1, REV-5, Administration of Insured Home Mortgages, Mortgage Letter 2001-19, Single Family Foreclosure Policy and Procedural Changes, or subsequent guidance, if any. As a reminder, under no circumstances will the mortgagor be required to pay the mortgagee more than the Department identified as customary and reasonable for claim purposes.

Although HUD does not prescribe a lien priority requirement for partial claims, the mortgagee must ensure timely recordation of the subordinate mortgage.

G. Repayment Terms

The partial claim advance will be secured by a note and subordinate mortgage with the following repayment terms:

- The note is interest free. (The Secretary reserves the right to assess interest on partial claim notes originated in the future.);
- No monthly or periodic payments are required, however, mortgagors may voluntarily submit partial payments;
- The note is due at the earlier of 1) the payoff of the first mortgage, or 2) when the

- mortgagor no longer owns the property;
- There is no prepayment penalty;
 - A mortgagor is only eligible to apply for a mortgage insurance premium (MIP) refund when the partial claim note has been paid in full;
 - The Partial Claim Note and security documents must be payable to HUD;
 - Voluntary payments or prepayments should be delivered via a cashier's check or other certified funds to the Department's servicing contractor at the following address.

U.S. Department of HUD
c/o First Madison Services, Inc.
4111 South Darlington
Suite 300
Tulsa, OK 74135

H. Required Documentation

A promissory note must be executed in the name of the Secretary and a subordinate mortgage must be obtained and recorded. The mortgagee must include the provisions of HUD's model form of note and subordinate mortgage (as provided in ML 97-17) and make any amendments required by state laws. While HUD does not endorse the products or services of vendors, the Department is aware that state specific documents are commercially available. Mortgagees who take advantage of the convenience of purchasing these documents should review them prior to use.

I. Disclosures

FHA requires mortgagees to comply with any disclosure or notice requirements applicable under State or Federal law.

J. Use of Pre-Foreclosure Sale where a Partial Claim was provided on an earlier default

Some mortgagees have erroneously failed to include the amount of the Partial Claim when calculating total indebtedness for the purpose of a pre-foreclosure sale. In order to be in compliance, mortgagees must include both the first mortgage and the partial claim amounts to correctly calculate the total outstanding mortgage indebtedness.

K. Loan Payoff or Refinance- Mortgagee Responsibilities

Mortgagees will be responsible for notifying HUD when the first mortgage is being paid in full or refinanced in order for HUD to provide a payoff figure on the Partial Claim. HUD's Servicing Contractor, identified in Section G of this mortgagee letter, should be contacted to request a payoff quote on the outstanding Partial Claim. The purpose of this requirement is to ensure that no partial claim is overlooked when preparations are made to pay the first mortgage in full.

L. Mortgage Incentives

FHA will pay mortgagees a \$250 incentive fee for each partial claim. The mortgagor may not be charged any additional costs for receiving this loss mitigation workout option, however, it is acceptable that legal costs and fees related to a canceled foreclosure action may be collected directly from the mortgagor. Mortgagees are reminded that all such costs must be reflective of work actually completed to the date of the foreclosure cancellation and the attorney fees may not be in excess of the fees that HUD has identified as customary and reasonable for claim purposes. Please refer to Mortgagee Letter 2001-19, issued August 24, 2001, or subsequent issuance, if any, for guidance.

M. Failure by the mortgagor on a Partial Claim

In the event the mortgagor becomes delinquent following reinstatement via a partial claim, it shall be treated as a new default and serviced accordingly.

N. Limitations on Use

If a loan has been modified or reinstated using a partial claim within the past three years, re-default risk is presumed to increase following a subsequent partial claim. Prior to allowing a partial claim in this circumstance, the mortgagee must prepare a written justification, and retain a copy along with supporting documents in the claim review file. It is anticipated that this will be a highly unusual occurrence, and that the cause of the second default will be unrelated to the original problem. There is a lifetime limitation of 12 monthly installments of PITI. **Once 12 full monthly installments have been paid by HUD on a claim type 33 (partial claim) for a given case number, no further partial claims will be honored on a specific case.**

O. Recordation Requirements

Upon execution of a partial claim by a mortgagor, the Department requires that the partial claim security instruments be submitted for recordation to the appropriate jurisdiction within a maximum period of five (5) business days following the execution **AND** prior to filing a claim with HUD.

The responsibility for servicing of the Partial Claim remains with the mortgagee until the security interests are legally recorded in the appropriate jurisdiction.

P. Claim Filing

In accordance with 24 CFR 203.371 (d) "along with the prescribed application for partial claim insurance benefits, the mortgagee shall forward to HUD the original credit and security instruments requirements by paragraph (c) of this section." Provided that the mortgagee has complied with the regulations, the mortgagee must file the claim within 60 days of the date the subordinate lien to HUD is executed. The claim may include the

amount of the partial claim note and the \$250 incentive fee. HUD will pay no other costs or fees. **Failure to file the claim within 60 days will result in loss of the \$250 incentive fee.**

Q. Document Delivery

It is the responsibility of the mortgagee to deliver the original promissory note and recorded mortgage to HUD's servicing contractor's business address listed in Section G of this Mortgage Letter, as soon as possible, but in any case, no later than six (6) months from the execution date of the partial claim note and security instruments.

HUD expects the mortgagee or its agent to periodically check on the status of all unreturned recorded documents and that mortgagees advise HUD of all such delayed deliveries. Where it appears that recorded documents cannot be forwarded due to delays in the land records office, mortgagees must request an extension of time. HUD's National Servicing Center (NSC) shall grant time extensions in the event document delivery is delayed by events beyond the control of the mortgagee. Except in extreme circumstances, late requests will be denied.

HUD Form 50012 is to be used for extension requests. Box 7, titled "Other" (specify) must be checked and the following wording is recommended for specification purposes: "Requesting an extension of time to return recorded Partial Claim documents to HUD" and must enter the number of days needed. Under the sections "Basis for Extension Request", the mortgagee must indicate the reason for the delay.

R. One-Time Amnesty for accepting outstanding Partial Claim related legal documents without penalty.

HUD shall provide a "One-Time Amnesty" to allow mortgagees to submit overdue Partial Claim documents without penalty. The Department is emphasizing HUD's willingness to partner with the mortgage industry on overdue partial claim related legal documents that remain outstanding because of a delay in receipt of recorded documents.

HUD expects mortgagees to exercise prudent and consistent diligence to ensure that all documents are promptly submitted for recordation and are then forwarded to HUD as required. HUD will accept *without penalty*, all overdue partial claim documents received within 45 days of the issuance date of this Mortgage Letter. Once the 45-day grace period has expired, on the 46th day HUD will begin issuing demand letters for the submission of overdue partial claim security instruments and notes and reimbursement of related incentives paid.

Any questions regarding this Mortgage Letter may be directed to HUD's National Servicing Center (NSC) at (888) 297-8685 or hsg-lossmit@hud.gov. These clarifications are effective immediately.

John C. Weicher
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Federal Housing Commissioner