

*Announcement 04-06*

*September 28, 2004*

*Amends these Guides: Selling and Servicing*

*Authoritative Online Selling and Servicing Guides, Purchase of Massachusetts “High Cost Home Mortgage Loans,” Mortgage Loan Documents, Arbitration, Waiver of Prepayment Premium, Guaranty Fees, and Escrow Accounts*

This Announcement includes several Selling and Servicing Guide topics that clarify or amend our current requirements or update policies that have been impacted by recent state laws. The topics addressed in this Announcement are:

- information on authoritative online Fannie Mae Selling and Servicing Guides and elimination of complimentary subscriptions for print versions,
- Massachusetts’ laws concerning “high cost home mortgage loans,”
- mortgage loan documents in Microsoft® Word format,
- arbitration policies,
- prepayment premium policy when a home is sold,
- guaranty fees, and
- escrow deposit accounts and administration.

### **Authoritative Online Selling and Servicing Guides**

[Selling Guide Part I: Lender Relationships; Chapter 2, Contractual Relationship; Section 201, Mortgage Selling and Servicing Contract and Servicing Guide Part I: Lender Relationships; Chapter 2, Contractual Relationship; Section 201, Mortgage Selling and Servicing Contract.](#)

Over the last few years, Fannie Mae has increased the accessibility and usability of the Single-Family Selling and Servicing Guides, Lender Announcements, and other lender

communications. We make Lender Announcements immediately available online on eFannieMae.com. Further, we have partnered with AllRegs® to provide authoritative, dynamic versions of these communications on eFannieMae.com that are searchable and printable.

Now that a great many of lenders' employees have access to these materials from their desktops, effective October 1, 2004, we will no longer provide complimentary print subscriptions to the Selling Guide, Servicing Guide, Lender Announcements, Lender Letters, or other lender communications relating to the Selling or Servicing Guide. Those lenders that have a current complimentary print subscription will continue to receive print versions of these documents through the end of the current subscription year, December 31, 2004. All of these documents will continue to be available electronically to lenders and others at no cost through eFannieMae.com, and free subscriptions to an email service that will provide notice of the posting of new lender communications also will be available through eFannieMae.com. Enclosed with this Announcement is a brochure that contains important information regarding enhancements we are planning for our Lender Announcements and Guide Updates and an information sheet that includes pricing and ordering information from our print distributor should you desire to continue to receive printed versions of these documents.

As a result, the following is added as a new paragraph at the end of Part I, Section 201 of the Selling Guide and the Servicing Guide:

Fannie Mae transmits lender communications to a lender by posting them on or making them available through Fannie Mae's official corporate Web sites FannieMae.com or eFannieMae.com (or such other Web sites as Fannie Mae may establish in the future) or by mailing printed copies for a fee. We require lenders to be informed of our Guide requirements and changes thereto, and lenders should select and rely on the manner of receiving notice of lender communications that best meets their business needs.

## Selling Guide

### **Purchase of Massachusetts “High Cost Home Mortgage Loans”**

Over the past few years, Fannie Mae and its lender partners have worked together to expand affordable homeownership, promote responsible lending practices, and combat predatory lending. Among those efforts are our standards to guard against the purchase of home mortgage loans with predatory features that were announced in Lender Letter 03-00, which includes a prohibition against the purchase of “high-cost” mortgage loans under the federal Home Ownership and Equity Protection Act (HOEPA). In that same vein, in Announcements 02-12, 03-02, 03-07, and 03-12 we announced that we would not purchase any mortgage loans that qualify as “high-cost home loans” or “high-risk home loans” under the Georgia Fair Lending Act, New York Banking Law §6-l, Kentucky statute §360.001, Arkansas Home Loan Protection Act, New Jersey Home Ownership Security Act of 2002, New Mexico Home Loan Protection Act, and Illinois High-Risk Home Loan Act.

The Massachusetts Predatory Home Loan Practices Act (Mass. Ann. Laws ch. 183C) will become effective November 7, 2004. The Massachusetts law applies to owner-occupied home loans secured by property located in the Commonwealth of Massachusetts. Effective November 7, 2004, mortgage loans may not be delivered to us if they qualify as “high cost home mortgage loans” under the Massachusetts law.

Pursuant to our Mortgage Selling and Servicing Contract, a seller represents and warrants that each mortgage loan it delivers conforms to all applicable requirements of our Selling Guide, which in the case of mortgage loans secured by Massachusetts property includes the prohibition on delivery of “high cost home mortgage loans” (as defined by the laws of Massachusetts), which is added to our Selling Guide by this Announcement. We expect a lender that sells us any loan secured by a Massachusetts property to have in place a process based upon the unique requirements of the Massachusetts law to ensure that it does not inadvertently deliver “high cost home mortgage loans” to us.

In addition, Fannie Mae will conduct quality assurance reviews of mortgage loans secured by properties in Massachusetts and will require repurchase of any determined to be “high cost home mortgage loans.”

### **Legal Documents in Word Format**

For the convenience of users, we are now posting all of the mortgage documents in Word format to [www.efanniemae.com/singlefamily/forms\\_guidelines/mortgagedocuments](http://www.efanniemae.com/singlefamily/forms_guidelines/mortgagedocuments). Fannie Mae will continue to post the PDF version of the documents in addition to the Word version. Users are reminded that changes to the mortgage documents should only be made as specifically authorized by Fannie Mae in the summary page to each document, or pursuant to our blanket authorization that permits changes made in connection with local recording requirements, or to reformat, add logos, include notices, and so forth. Users making unauthorized changes are subject to nonstandard document warranties and are required to edit the tagline to indicate that the document has been modified and by whom, i.e.

“modified by XYZ Lender.” In the alternative, users may create a second tagline to include this attribution language.

## **Arbitration**

A significant part of our effort to create sustainable homeownership opportunities is the re-examination of Fannie Mae’s standards for loans we purchase or securitize. The policies outlined below relating to arbitration derive from our commitment to ensure that the terms and conditions of mortgages and other agreements are fair and balanced for all parties in the transaction.

Part IV: Mortgage Documents; Chapter 1, Security Instruments; Section 102.01, First Mortgage Security Instruments. This section of the Selling Guide states that our standard security instruments do not include language that provides for arbitration, and our authorized changes to those documents do not permit the addition of arbitration language. The Selling Guide further states that a mortgage that is subject to arbitration - regardless of whether the arbitration language has been added to the security instrument or is part of a separate agreement - is not acceptable under our standard terms.

We recognize that arbitration potentially represents a more efficient, streamlined, and less costly process to borrowers for resolving disputes than litigation. We also recognize, however, that borrowers who would prefer to present their grievances in court may unknowingly agree to mandatory arbitration at the time they sign their mortgage documents. Mandatory arbitration provisions are loan provisions or an agreement accompanying the loan that require the borrower to submit to arbitration any disputes arising out of or relating in any way to the mortgage loan transaction. While Fannie Mae does not believe arbitration provisions are inherently abusive, we believe that mandatory arbitration can be used in an abusive fashion.

Therefore, mortgage loans that are subject to mandatory arbitration are ineligible for sale to, or securitization by, Fannie Mae. The only exception to this policy is when the mandatory arbitration provision also contains a waiver provision that provides that, in the event of a transfer or sale of the mortgage loan or an interest in the mortgage loan to Fannie Mae, the mandatory arbitration clause immediately and automatically becomes null and void and cannot be reinstated. Neither the seller nor the servicer can require that the borrower submit to arbitration to resolve any dispute arising out of or relating in any way to the mortgage loan transaction. The seller will provide the borrower with written notice of the triggering of the waiver provision within 60 days of the transfer or sale of the mortgage loan or an interest in the mortgage loan to Fannie Mae, which notice will contain substantially the following language:

Pursuant to your mortgage loan documents, we are hereby notifying you that an interest in your loan has been transferred or sold to Fannie Mae and therefore the mandatory arbitration clause of your loan, requiring that you submit to arbitration to resolve any dispute arising out of or relating in any way to your mortgage loan, is immediately null and void.

The seller and servicer shall maintain a copy of such notice in the mortgage file.

Finally, lenders are reminded of their selling warranty that all loans delivered to Fannie Mae (regardless of documentation used) are enforceable in accordance with their terms. Further, loans sold to us that provide for mandatory arbitration and the waiver described above are nonstandard documents. Therefore, the lender makes our nonstandard document selling warranties when it delivers such loans. (Please see Selling Guide Part I, Section 202.01, Subpart B.)

These requirements will apply to all loans closed on or after October 31, 2004.

## **Waiver of Prepayment Premium Upon Borrower's Sale of Home**

Part IV: Mortgage Documents; Chapter 2, Mortgage or Deed of Trust Notes; Section 201.02, Prepayment Provision. In Announcement 04-03, we discussed our criteria for mortgage loans that contain prepayment premiums. In that discussion, we encouraged lenders to agree to waive all or part of a prepayment premium if a prepayment premium is required because the home is sold. Along with this provision, we included a requirement that at the time of Fannie Mae purchase or securitization, lenders must elect whether to waive all or part of the prepayment premium in the event the home is sold, and must notify the borrower if they elect to waive the premium.

It has been brought to our attention that the required election and notification at the time of purchase or securitization is operationally difficult for many lenders, and may be an impediment to the practice of allowing this waiver. Therefore, we are eliminating the election and borrower notification requirements at the time the loan is sold to or securitized by Fannie Mae, effective immediately.

It is our hope that by making this provision easier for lenders to comply with, more lenders will follow our encouragement and offer a waiver of the prepayment premium to borrowers at the time the home is sold.

## **Guaranty Fees**

Part II: Delivery Options; Chapter 2, MBS Pool Deliveries; Section 203, Guaranty Fees. We are revising Sections 203, 203.01, 203.02, 203.03, and 203.04 of the Selling Guide to update and clarify our policies on Guaranty Fees. The following text replaces those Sections in their entirety effective immediately:

### **Section 203: Guaranty Fees**

The lender must pay Fannie Mae a guaranty fee remittance each month as compensation for the lender's right to participate in the MBS program. The guaranty fee remittance rate for MBS pool mortgages varies depending on the credit risk of mortgages included in the

pool, the servicing option that applies to each mortgage in the pool, and the remittance cycle that applies to the pool. The guaranty fee is a corporate responsibility of the servicer and is not a function of the pool cash flows; therefore, it must be paid even if there is no pool collection activity.

The specific guaranty fee applicable to an MBS pool mortgage loan is set forth in the related MBS pool purchase contract between Fannie Mae and the lender.

### **Section 203.01: Guaranty Fee for Standard Remittance Cycle**

The guaranty fee agreed to by the lender and Fannie Mae (and reflected in the applicable MBS pool purchase contract) normally assumes that the lender will remit under the standard remittance cycle. The lender and Fannie Mae may agree on a different remittance cycle, either MBS Express® or Rapid Payment Method® remittance, and the MBS pool purchase contract and guaranty fee will be revised to reflect the appropriate remittance cycle.

### **Section 203.02: Guaranty Fee for Rapid Payment Method Remittance Cycle**

The guaranty fee for mortgage loans in an MBS pool that have the Rapid Payment Method remittance cycle can be lower or higher than the guaranty fee for pools that have the standard remittance cycle because this remittance cycle results in Fannie Mae receiving principal (scheduled and unscheduled) and interest funds earlier or later in the month. Once the lender selects the Rapid Payment Method remittance cycle for mortgage loans to be delivered under a specific MBS pool purchase contract, the Rapid Payment Method is mandatory for all deliveries made under that MBS pool purchase contract. The exact guaranty fee adjustment that will apply to MBS pools that have the Rapid Payment Method remittance cycle will vary over time based on various market economic factors and date of remittance. A lender interested in using the Rapid Payment Method remittance cycle should contact its Fannie Mae Customer Account Manager to determine the guaranty fee rates currently in effect.

### **Section 203.03: Guaranty Fee for MBS Express Remittance Cycle**

The guaranty fee for mortgage loans in an MBS pool that has the MBS Express remittance cycle is typically lower than that for pools that have the standard remittance cycle because the MBS Express remittance cycle results in Fannie Mae receiving unscheduled principal earlier in the month. Once the lender selects the MBS Express remittance cycle under a specific MBS pool purchase contract, the MBS Express remittance cycle is mandatory for all deliveries made under that MBS pool purchase contract. The exact guaranty fee adjustment that will apply to MBS pools that have the MBS Express remittance cycle will vary over time based on various market economic factors and also on product type. A lender interested in using the MBS Express remittance cycle should contact its Fannie Mae Customer Account Manager to determine the guaranty fee rates currently in effect.

## Section 203.04: Payment of Guaranty Fee

The guaranty fee remittance for MBS pools is based upon a weighted-average guaranty fee factor. The annualized weighted-average guaranty fee factor for a pool (expressed in basis points) is determined by multiplying the issue date principal balance of each mortgage loan in the pool (or, in subsequent months, the “scheduled” balance of each mortgage loan) by the applicable guaranty fee rate for the mortgage loan expressed in basis points (adjusted for any remittance cycle adjustments, buyup, or buydown, if applicable), summing the products of all the mortgage loans in the pool, dividing that sum by the aggregate issue date principal balance for the pool (or, in subsequent months, by the “scheduled” security balance for the pool) and rounding the result to the nearest hundredth of a basis point. The aggregate issue date principal balance of the pool (or, in subsequent months, the scheduled security balance for the pool) is then multiplied by the annualized weighted-average guaranty fee factor (expressed in basis points), divided by 120000, and rounded to two decimal places to determine the monthly guaranty fee remittance for the pool.

On the 7th day of each month (or, if the 7th is a holiday or weekend, on the preceding business day), Fannie Mae will draft guaranty fee remittances from the custodial bank account the lender designates as its draft account. If the guaranty fee remittance is to be drafted from the lender’s P & I custodial account for MBS pools, the lender must make sure that it does not withdraw the guaranty fee remittance when it takes its monthly servicing fee from the account. (Please see Servicing Guide Part IX: Custodial and Remittance Accounting, for more information about designating bank accounts for drafting purposes and confirming guaranty fee remittances.)

## Escrow Deposit Accounts

We are modifying our policies on escrow deposit accounts and escrow administration in our Selling and Servicing Guides to strengthen our efforts to create sustainable homeownership opportunities. These efforts are an integral part of our expanded *American Dream Commitment*® plan launched earlier this year.

Part VII: Mortgage Eligibility; Chapter 1, Conventional Mortgages; Section 104.05, Mortgage Payments. The Selling Guide states that the lender may waive the escrow deposit account requirement for an individual first mortgage loan, as long as the standard escrow provision remains in the mortgage documents and can be reinstated in appropriate circumstances. However, we do not recommend waiving escrows for a borrower who has a blemished credit record because the borrower may find it difficult to maintain homeownership if he or she is faced with the need to make lump-sum payments for taxes and/or insurance and any other periodic payment items. A lender should not make a practice of rarely or never establishing escrows for blemished credit borrowers with the intent of understating the true cost of financing and generating fees out of activities like lender-placed insurance.

If a lender permits escrow waivers, then (subject to the mortgage documents and applicable law) the lender’s written policies should provide that the waiver not be based solely on the

loan-to-value ratio of a loan, but also on whether the borrower has the financial ability to handle the lump-sum payment of taxes and insurance. For example, financial ability could be found to exist when the borrower has had an acceptable payment history on a previous mortgage loan.

We encourage lenders to provide all borrowers with a timely, clearly written disclosure that advises them of the implications of not establishing an escrow account, particularly

- informing borrowers of any applicable fees associated with the waiver of escrows;
- advising borrowers that they are responsible for personally and directly paying the non-escrowed items, in addition to paying the mortgage loan payment; and
- explaining the consequences of a failure to pay non-escrowed items, including the requirement for lender placement of insurance and the potentially higher cost (including any potential commission payments to the lender) and/or reduced coverage for borrowers of lender-placed insurance.

These policies apply to all loans closed on or after January 1, 2005.

## Servicing Guide

### **Escrow Administration**

Part III: General Servicing Functions; Chapter 1, Mortgage Payments; Section 103.01, Waiver of Escrow Deposits and Chapter 2, Taxes and Assessments; Section 201, Taxes and Ground Rents. Subsequent to the origination and sale of a loan to us, we require servicers to begin escrowing taxes and insurance when a borrower fails to pay taxes and insurance when due.

Similarly, in connection with a workout arrangement to address a principal and interest delinquency, we expect a servicer to consider the merits of also addressing any impending tax and insurance payment associated with a non-escrowed mortgage as part of the workout and determine whether establishing an escrow account would be advisable.

In the case of a borrower for whom a servicer mandates that an escrow account be established subsequent to loan origination, if the borrower appears unable to pay any outstanding amounts due, the servicer should advance the payment and schedule out the repayment of that amount over as much as 12 months (or longer if the servicer deems appropriate). If, however, it appears that the borrower will not have the ability to become current on taxes and/or insurance even with the benefit of such “scheduling-out,” other loss mitigation steps should be pursued to arrange for the collection of the outstanding amounts owed.

Periodically, borrowers of an escrowed loan who are current in their mortgage obligation will ask to be moved to a non-escrowed status. If a servicer permits escrow waivers, then (subject to the mortgage documents and applicable law) the servicer’s written policies should provide that the waiver not be based solely on the loan-to-value ratio of a loan, but also on whether the borrower has the financial ability to handle the lump-sum payment of taxes and insurance. Financial ability could be found to exist, for example, when the borrower has had an acceptable payment history on his or her mortgage.

When a waiver request has been granted, we encourage servicers to provide the borrower with a timely, clearly written disclosure that advises them of the implications of waiving the escrow account, particularly:

- informing borrowers of any applicable fees associated with the waiver of escrows;
- advising borrowers that they are responsible for personally and directly paying the non-escrowed items, in addition to paying the mortgage loan payment; and
- explaining the consequences of a failure to pay non-escrowed items, including the requirement for lender placement of insurance and the potentially higher cost (including any potential commission payments to the servicer) and/or reduced coverage for borrowers of lender-placed insurance.

Servicers must also include in the borrower’s record (and make available for our inspection, if requested) the borrower’s request and the basis for the decision to approve any such waiver.

Servicers will have until January 1, 2005 to implement these servicing policies, although they are encouraged to do so as expeditiously as possible.

\*\*\*\*\*

We appreciate the advice and support we have received from many of our lending and servicing partners regarding these changes. Many of these changes represent best practices that have already been widely adopted by our business partners.

Lenders who have questions about this Announcement should contact their Customer Account Manager.

Pamela S. Johnson  
Senior Vice President