

MEMO



Date: July 1, 2013
To: Members
From: Community Investment Department
Subject: HUD Interpretive Rule: Prohibited Sources of Minimum Cash Investment and Mortgagee Letter 2013-14

The Federal Home Loan Bank of Des Moines ("Bank") provides down payment and closing cost assistance to prospective homeowners through our Affordable Housing Program ("AHP"), Homeownership Set-Aside Programs (Homeownership Fund, Native American Homeownership Initiative, Urban First Time Homebuyers Fund, and Rural Homeownership Fund). The Federal Home Loan Banks, a government sponsored enterprise, have been regarded by HUD as an "instrumentality of government" for purposes of providing secondary financing for down payment assistance to prospective homeowners (re: HUD issued Mortgagee Letter 94-2, issued January 11, 1994). In addition, the Federal Home Loan Bank's Set-Aside Program is an acceptable source of funds that may be used in conjunction with FHA-insured financing to satisfy a borrower's Minimum Cash Investment requirement, per HUD Handbook 4155.1 Section 5.B.7.d.

On December 5, 2012, HUD published an Interpretive Rule, Docket No. FR-5679-N-01. This rule expressed HUD's interpretation that Section 203(b)(9)(C) of the National Housing Act does not prohibit FHA from insuring mortgages originated as part of the homeownership programs of Federal, State, or local government or their agencies or instrumentalities when the government entities also *directly* provide funds toward a borrower's required Minimum Cash Investment. Due to the variety and complexity of laws governing the conduct of government entities, HUD issued Mortgagee Letter 2013-14, with an effective date of July 1, 2013, to streamline the process for directly providing funds for the government entity in FHA-insured transactions.

The Bank's Set-Aside funds are provided to our Members under the legal framework of an Affordable Housing Program Agreement ("Agreement"). The Agreement demonstrates that the Bank provided these funds through the creation of a legal liability or obligation. To establish that the Bank provided a borrower's Minimum Cash Investment in a manner consistent with HUD's Interpretive Rule, we will provide a letter, signed by authorized staff of the Community Investment Department, establishing that the funds legally belonged to us at or prior to closing. This letter is acceptable documentation to demonstrate that the Bank directly provided these funds for a borrower's required Minimum Cash Investment, per HUD's Mortgagee Letter 2013-14. An example of that letter and HUD's Mortgagee Letter 2013-14 are attached.

To obtain an FHA Minimum Cash Investment Letter the Member should request it from the Bank prior to or after closing applicable FHA financing. The Member must identify the borrower and provide the borrower's address. Members should be advised that this letter does not change the requirements of the Member under the Agreement and the applicable AHP. For the Member to receive funds from the Bank, they must be in compliance with the Agreement and the requirements of the AHP.

To obtain an FHA Minimum Cash Investment Letter, contact Evelyn Bengtson at 1-800-544-3452, extension 1064.



Date

Name
Title
Address
City, State Zip

Dear (Name),

This letter is to advise that the Federal Home Loan Bank of Des Moines ("Bank") and ("Member") have entered into an Affordable Housing Program Agreement ("Agreement") with the effective date of . The Federal Home Loan Bank's Affordable Housing Program ("AHP") is an acceptable source of funds that may be used in conjunction with FHA-insured financing to satisfy a borrower's Minimum Cash Investment requirement, per HUD Handbook 4155.1 Section 5.B.7.d. The reader is advised that this Agreement creates a legally enforceable obligation for the Bank to provide the Member funds towards an eligible homebuyer's downpayment and/or closing costs for the purchase of an owner-occupied residence, provided the Member complies with the terms of the Agreement. The funds provided the borrower will be subject to the terms of an AHP Retention Agreement on the residence in compliance with FHA requirements at 24 CFR 203.41 and Mortgagee letter 94-02, and AHP regulations codified as 12 C.F.R. Part 1291 and the directives of the Federal Housing Finance Agency.

The Bank hereby acknowledges that the Member has made or will make a first mortgage FHA-insured loan ("FHA First Lien Loan") to ("borrower") for purchase of an owner-occupied residence whose address is . Further, the Member has made or will make available to the borrower funds from the Agreement which represent the borrower's Minimum Cash Investment for an FHA First Lien Loan.

Sincerely,

Name
Title
Federal Home Loan Bank of Des Moines



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

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

Date: May 9, 2013

To: All FHA-Approved Mortgagees

Mortgagee Letter 2013-14

Subject Minimum Cash Investment and Secondary Financing Requirements – Acceptable Documentation for Funds Provided by Federal, State, or Local Governments, their Agencies or Instrumentalities

Purpose This Mortgagee Letter sets forth the documentation mortgagees must provide to demonstrate eligibility for FHA mortgage insurance of loans when a Federal, State, or local government, its agency or instrumentality directly provides the borrower's required Minimum Cash Investment in accordance with the principles set forth in the December 5, 2012 Interpretive Rule ("Interpretive Rule"), Docket No. FR-5679-N-01.

This Mortgagee Letter also provides mortgagees with guidance on resolving concerns with extending secondary financing by the Federal, State, or local government, its agency or instrumentality when those entities provide the borrower's required Minimum Cash Investment through secondary financing.

Effective Date This Mortgagee Letter is effective July 1, 2013.

Affected Topics HUD Handbook 4155.1 Sections 5.B.1.a, 5.C.2.c, 5.B.5.b and Mortgagee Letter 2008-23 are affected by this guidance. The changes will be integrated into the FHA Single Family On-Line Handbooks.

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Mortgage Letter 2013-14, Continued

Background The originating FHA-approved mortgagee must document that all funds for the borrower's required Minimum Cash Investment necessary to close the FHA-insured mortgage belong to the borrower or were provided by a permissible source in accordance with FHA requirements. Section 2113 of the Housing and Economic Recovery Act of 2008 (HERA), amended section 203(b)(9) of the National Housing Act (NHA). This amendment requires the borrower to provide a required Minimum Cash Investment equal to but not less than 3.5 percent of the appraised value of the property. None of this required minimum cash investment can be provided by the seller of the property or any other person or entity who financially benefits from the transaction, or from any person who is reimbursed by any prohibited source. Mortgagees must ensure compliance with sections 203(b)(9)(A) and (C) of the NHA in order for the borrower's mortgage to be eligible for FHA insurance.

On December 5, 2012, HUD published an Interpretive Rule, Docket No. FR-5679-N-01. This rule expressed HUD's interpretation that section 203(b)(9)(C) of the NHA does not prohibit FHA from insuring mortgages originated as part of the homeownership programs of Federal, State, or local government or their agencies or instrumentalities (hereinafter referred to as "Government Entities") when the Government Entities also directly provide funds toward the required Minimum Cash Investment.

Additionally, HUD's requirements have historically required all secondary financing being put in place by Government Entities to be "made" by the Government Entity. However, due to the variety and complexity of state and local laws governing the conduct of these types of Government Entities, FHA will streamline this process for the Government Entity in FHA-insured transactions.

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Mortgagee Letter 2013-14, Continued

Acceptable Documentation

To establish that the Government Entity provided the borrower's required Minimum Cash Investment in a manner consistent with HUD's Interpretive Rule, the mortgagee must document that the Government Entity incurred prior to or at closing an enforceable legal liability or obligation to fund the borrower's required Minimum Cash Investment. While it is not sufficient to document that the Government Entity has agreed to reimburse the lender for the use of funds legally belonging to the lender to fund the borrower's required Minimum Cash Investment, the documentation described below will demonstrate that the Government Entity's funds, generated through the creation of a legal liability or obligation were the permissible source of the required Minimum Cash Investment.

Acceptable forms of documentation include the following:

- A cancelled check, evidence of wire transfer or other draw request showing that prior to or at the time of closing the Government Entity had authorized a draw of the funds on its account provided towards the borrower's required Minimum Cash Investment from the Government Entity's account; or
- A letter from the Government Entity, signed by an authorized official, establishing that the funds provided towards the borrower's required Minimum Cash Investment were funds legally belonging to the Government Entity at or before closing.

Where a letter from the Government Entity is submitted, the precise language of the letter may vary because of differences in the funding and legal authority of each Government Entity. Examples of acceptable language, which would establish the funds were legally belonging to the Government Entity, would include the following:

- A statement that the Government Entity has, at or before closing, incurred a **legally enforceable liability** as a result of its agreement to provide the funds towards the borrower's required Minimum Cash Investment;
- A statement that the Government Entity has, at or before closing, incurred a **legally enforceable obligation** to provide the funds towards the borrower's required Minimum Cash Investment; or
- A statement that the Government Entity has, at or before closing, authorized a draw on its account to provide the funds towards the borrower's required Minimum Cash Investment.

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Mortgagee Letter 2013-14, Continued

Acceptable Documentation *(continued)*

The mortgagee is not required to document the actual transfer of funds in satisfaction of the obligation or liability, which resulted from the funding of the borrower's required Minimum Cash Investment by the Government Entity, before closing, provided the mortgagee has obtained documentation that a legally enforceable liability or obligation was incurred at or before closing. Where such documentation is provided establishing that a legally enforceable liability or obligation was incurred at or before closing, the funds provided at closing for down payment assistance will be considered by HUD to be funds legally belonging to the Government Entity. However, failure of the Government Entity to satisfy the obligation or liability may result in a determination that the funds were provided by a prohibited source.

Note: The Mortgagee is reminded to document a Gift Letter for the borrower's Cash to close including the required Minimum Cash Investment as described in HUD Handbook 4155.1 5.B.5.a **Gift Letter Requirement**. The Mortgagee must place the Gift Letter and the documentation evidencing the provision of the borrower's required Minimum Cash Investment in compliance with the Interpretative Rule on the right side of the endorsement binder with Asset Verification documentation needed to close. These instructions on the placement of documentation in the endorsement file supersede the guidance in 4155.1 5.B.5.b.

Making of Secondary Financing On behalf of Government Entities

FHA recognizes the importance of compliance with state and local law to the conduct of any Government Entity providing down payment assistance in the form of secondary financing. Where the Government Entity cannot legally or operationally ensure that secondary financing is "made" by the Government Entity, FHA will permit the secondary financing component to be made by an FHA-approved mortgagee or FHA-approved non-profit on behalf of the Governmental Entity provided the mortgagee or non-profit is not a prohibited source and the Government Entity holds the secondary financing prior to endorsement of the first mortgage for FHA insurance until further notice. Mortgagees must document that the secondary financing is held by the Government Entity prior to submission of the mortgage to HUD via the Direct Endorsement process for insurance, or the endorsement of the mortgage for insurance through the Lender Insurance process.

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Mortgagee Letter 2013-14, Continued

**Making of
Secondary
Financing
On behalf of
Government
Entities
(continued)**

All 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.

**Information
Collection
Requirements**

The information collection requirements contained in this document have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned an OMB control number of 2502-0059. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB Control Number.

Questions

Please inquire about information provided in this Mortgagee Letter by contacting FHA's Resource Center at 1-800-CALLFHA (1-800-225-5342). Persons with hearing or speech impairments may reach this number via by calling the Federal Information Relay Service at (800-877-8339). For additional information on this Mortgagee Letter, please visit www.hud.gov/answers.

Signature

Carol J. Galante

Assistant Secretary for Housing-Federal Housing Commissioner
