

## **HUD REOs**

### **Overview**

Through the Property Disposition Insured Sales Program, HUD offers its Real Estate Owned (REO) properties for sale with FHA-insured financing available. Properties must meet the intent of the FHA's Minimum Property Standards (MPS) for existing properties and Minimum Property Standards (MPS) for new construction to be eligible for this program.

### **Eligibility Requirements**

#### **Property Types**

Single-family dwellings

Planned Unit Developments (PUDs)

Site Condos

Condominiums (must be prior approved by FHA)

2-4 units

#### **Borrowers**

Individuals only.

#### **Occupancy**

Owner-occupied only.

### **HUD Marketing Approaches**

Each HUD REO property will be offered for sale using one of the approaches listed below.

**Insurable (203b):** Properties marketed as "insurable" are those that meet FHA's MPR for existing housing and MPS for new construction at the time of the appraisal in their "as-is" condition without repairs being necessary.

**Insurable with repair escrow (203b):** A property that requires no more than \$5,000 for repairs to meet FHA's MPR or MPS as estimated by the PCR and as reviewed and determined to be reasonable by the appraiser, is eligible to be marketed for sale in its "as-is" condition with FHA mortgage insurance under the 203(b) repair escrow program, provided the purchaser(s) establishes a cash escrow to ensure the completion of the required repairs. Purchaser(s) are permitted to include in their mortgage an amount equal to 110 percent of the estimated cost of the repairs. Note that, per Mortgagee Letter 2005-50, properties designated insurable with repair escrow (\$5,000 or less in required repairs) may also be eligible for the 203(k) Streamlined program, provided that the repairs qualify as eligible work items. See the 203(k) Guidelines for details.

**Uninsurable as 203b (may be eligible for 203k):**

Properties offered for sale “uninsured” do not meet, in their “as is” condition, FHA’s MPR or MPS and the cost of repairs identified by the appraiser to meet MPR or MPS are estimated to exceed \$5,000. Uninsurable properties may qualify for Section 203(k) financing and, depending on the scope and extent of repairs needed, the Streamlined 203(k) Limited Repair Program. Alternatively, the buyer may utilize non-FHA financing (Conv, VA, etc.) or pay cash.

**Review of the HUD Sales Contract**

(Refer to Mortgage Letter 00-27 for more information)

The HUD sales contract (form HUD-9548) must be fully completed and signed by the submitting selling broker, the M&M (Management & Marketing) Contractor and the prospective purchaser. If applicable, the Lead-Based Addendum may be attached. The HUD sales contract must specify the:

Sales price

Financing terms

Amount of closing costs HUD will pay at settlement

Real estate commission HUD will pay

Closing date

Discount on the sales price that will be provided at settlement (if any).

The "Radon Gas and Mold Notice and Release Agreement" must be included with sales contract and be fully executed by all purchasers of the subject property.

In order to qualify for FHA-insured financing, the first block on Line 4 of the sales contract, as well as the applicable block for the FHA program - 203(b), 203(b) repair escrow, or 203(k) - must be checked.

REO properties that are condominiums which are offered for sale with FHA mortgage insurance should be processed under Section 234(c), even though Section 203(b) is specified on the sales contract.

A specific down payment and mortgage amount is no longer required to be established on Line 4 of the sales contract. The purchaser(s) must, however, continue to indicate the type of financing being sought.

The amount on Line 5 of the sales contract represents actual borrower financing and closing costs to be paid on their behalf by HUD (the seller) out of the sales proceeds. It does not represent an amount which the borrower may finance in the mortgage.

Only the actual amount of closing and financing costs will be paid by HUD at settlement. The borrower will not be credited at settlement for any unused portion. Prepaid items may not be paid out of the amount on Line 5 (See HUD Notice 99-04).

Specified on Line 8 of the sales contract will be the percentage discount, if any, which will be applied to the sales price at settlement. Where the price will be discounted, the mortgage amount will be based on that discounted sales price, not the contract sales price.

Specified on Line 9 of the sales contract will be the number of days, normally 45 or 60, in which the sale must be closed.

If the contract is not complete, if there are questions about the terms or conditions or if the contract must be amended as a condition of loan approval, contact the M&M contractor.

Note: Site condominiums do not require FHA approval and must be processed under Section 203(b).

### **HUD REO Appraisal Requirements (ML 2010-08)** **HUD REO Appraisal Validity Period**

All appraisals utilized to establish the listing price on an REO property owned by HUD, with an effective date on or after April 1, 2010, will be valid for a period of 120 days from the effective date of the appraisal.

The HUD REO sales contract must be ratified within 120 days of the appraisal effective date or a new appraisal or an appraisal update in accordance with the guidance provided in ML 2009-51 to support the mortgage transaction is required.

### **REO Second Appraisals to Support a Higher Purchase Price**

With the exception of 203(k) as-repaired appraisals, when a buyer is using FHA financing to purchase a HUD REO property, the appraisal that was utilized in determining the list price will remain effective for purposes of obtaining the FHA-insured mortgage.

A second appraisal may not be ordered simply to support a purchase price that is higher than the value on the current appraisal. A second appraisal can only be ordered to support a higher sales price if there are material deficiencies with the current appraisal or the current appraisal will not be valid on the date of contract ratification. The DE underwriter is responsible for determining if there are material deficiencies with respect to the current appraisal and document why a second appraisal was ordered. The loan file must contain copies of both appraisals.

### **HUD REOs - CHUMS Processing a.k.a. FHA Connection**

A new FHA case number must be obtained for loan applications with FHA-insured financing involving REO properties. When entering the case information in FHA Connection, select "Real Estate Owned" for processing type.

When processing, the Computerized Homes Underwriting Management System (CHUMS) will require a response to the following question, "Was this case previously sold as a Property Disposition?"

**Always** check **YES** when processing a loan application for FHA-insured financing on an REO property.

The mortgagee should complete the "Previous Case Number" field. This field is designed to track REO properties sold with FHA-insured financing and whether they are subsequently sold by the individuals who purchased them from HUD.

If entry of the previous case number triggers an error message, the underwriter should request that the processing and underwriting division of their Homeownership Center (HOC) post the number in the CHUMS property disposition file.

**Note:** the appraisal fields in the FHA Connection should be left blank when obtaining a new case number for REO loans.

If the REO property is a condominium, FHA Connection will require the entry of the condo ID. If FHA financing was approved on the sales contract, the condominium development must be in compliance with the condominium procedures (ML 2009-46A and 2009-46B).

Note: Site condominiums do not require FHA approval and must be processed under Section 203(b).

### **HUD – REOs: Inspection Requirements** **Termite/Pest Inspection**

A termite inspection is required on existing property:

When called for in the sales or purchase agreement, or

When the appraiser recommends the inspection in the appraisal report.

A termite inspection is no longer an automatic inspection requirement (Mortgagee Letter 2005-48). The underwriter should contact the M&M contractor to determine if an inspection report has been performed, and, if it has, to obtain a copy of it.

### **Well and Septic System Inspections**

If the HUD REO property has a well and/or septic tank, underwriters should contact the M&M contractor to determine if an inspection has been performed, and, if it has, to obtain a free copy of this inspection report.

A septic test or inspection is required on existing property:

When called for in the sales or purchase agreement, or

When the appraiser recommends the inspection in the appraisal report.

A well test or inspection is required on existing property

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When called for in the sales or purchase agreement, or

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When the appraiser recommends the inspection in the appraisal report or

If there is knowledge that well water may be contaminated or

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When the water supply relies upon a water purification system due to presence of contaminants or

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When there is evidence of:

Corrosion of pipes (plumbing)

Areas of intensive agriculture within 1/4 mile

Coal mining or gas drilling operations within 1/4 mile

Dump, junkyard, landfill, factory, gas station, or dry cleaning operation within 1/4 mile

Unusually objectionable taste, smell or appearance of well water (superseding the guidance in mortgagee letter 95-34 that requires well water testing in the absence of local or state regulations)

In cases where well tests are necessary as described above, FHA's existing testing standards outlined in Chapter 3, Paragraph 3-6, A-5a of Handbook 4150.2 remain in effect and supersede Mortgagee Letter 95-34.

**Note:** Arrangements should be made with the M&M contractor for any required testing to be completed.

### **HUD – REOs: Inspection Requirements, Continued** **Home Inspection**

The borrower has the right to have the house inspected by a professional home inspector. HUD's M&M contractor shall permit entry to the purchaser(s) during the contract period to activate the utilities for the purposes of conducting a home inspection. If the HUD REO appraisal was completed without the utilities being activated, the underwriter or purchaser(s) must complete the systems check while the utilities are activated.

Additionally, where FHA-insured financing is specified on the sales contract, a form HUD-92564-CN, "For Your Protection: Get A Home Inspection," must be provided to prospective homebuyers at first contact, be it pre-qualification, pre-approval, or *no later than* initial application. If the form is incorporated within the executed sales contract in its entirety, then the homebuyer need not separately be provided with form HUD-92564-CN.

In the event the home inspection or the systems check reveals that repairs are needed which no longer makes the property eligible for an FHA-insured 203(b) mortgage, the underwriter should contact the M&M contractor to discuss alternatives to allow the sale to continue. The M&M contractor may allow the modification of the sales contract, as needed, to reflect either an insured with repair escrow sale or to an FHA 203(k) sale in those instances where the underwriter provides them with sufficient documentation to support the change in financing.

The sales contract must be revised to include this revision and initialed by both the purchaser and the M&M contractor.

In the event the purchaser(s) wishes to finance eligible rehabilitation in the purchase mortgage through a 203(k) mortgage but the property was listed as “insurable,” the underwriter should provide the M&M contractor with sufficient documentation to support the change in financing terms and obtain a modification to the sales contract.

### **HUD REOs: Down Payment**

The maximum mortgage amount and minimum cash investment must be calculated using the FHA Underwriting Transmittal.

### **Maximum Mortgage Calculation**

In performing the maximum mortgage calculation:

The Direct Endorsement Underwriter must enter on Line 1 1a. of form HUD-92900-PUR the lesser of the sales price or the “as-is” value specified on the contractor’s appraisal.

The mortgage amount may no longer be based solely on the sales price.

### **Additional Sales Incentives**

From time-to-time, for particular properties or in particular areas, HUD may authorize additional sales incentives. Where additional incentives are authorized, they will be noted in writing on either the HUD Sales Contract or on a cover letter accompanying the HUD sales contract.

For properties that HUD has approved with a \$100 down payment, the UFMIP may only be financed if the total loan amount does not exceed 100%\* based on the “as is” appraised value.

Where a discount on the sales prices is being provided, the mortgage amount shall be based on the lesser of the “as-is” value or the discounted sales prices, not the contract price.

Closing costs and prepaids may not be included in the mortgage. The Good Neighbor Next Door program is an exception.

**\*Note:** UFMIP may not be partially financed, therefore if the financed UFMIP will exceed 100%, the entire premium must be paid in cash from borrower funds.

### **HUD REO Closing Costs/Prepaid Expenses**

For HUD-paid closing costs, HUD has authorized as a sales incentive, purchasers to specify in Item 5 on the HUD sales contract an amount which HUD, as seller, may pay on the borrower’s behalf at settlement.

This amount may be applied to the **actual cost** of closing costs and/or prepaid expenses. If the total of actual costs of such closing costs and/or prepaid expenses is less than the amount specified in Item 5, the balance may not be credited to the borrower.

Depending upon the amount of closing costs that HUD pays for the borrower, the maximum mortgage amount may have to be reduced in order for the borrower to meet the minimum cash investment required.

### **Repair Escrow**

Properties that need less than \$5,000 worth of repairs to meet the intent of the MPS will be offered for sale with insured financing available, provided a cash escrow is established to ensure the completion of repairs.

### **Repair Escrow Financing**

The repair escrow must be financed in the FHA loan and is not to be taken from HUD proceeds at closing.

### **Escrow Account**

Equal to 110 percent of the estimated cost of repairs and must be established for properties sold under the Property Disposition Sales Program. Since the maximum cost of repairs is \$5,000, the maximum escrow amount may not exceed \$5,500.

### **Cost of Repairs**

Bidders are provided with a list of the repairs needed to make the property insurable and the estimated cost of repairs.

### **Inspections**

As part of the responsibility for administering the escrow account, as the lender, RMS must arrange and pay for the inspection of the completed repairs. RMS may use either the mortgagee certification procedure or request an inspection by the inspector under contract to inform the HUD Field Office that the work has been completed.

If a contract inspector inspection is requested, the underwriter must provide a copy of HUD's list of required repairs to the inspector. Payment for the inspection must come from the \$200 maximum allowable fee for establishing the escrow account.

### **Completion of Repairs**

Generally, all repairs are to be completed by the borrower within 90 days of closing.

If actual repair costs are less than the amount escrowed, the balance of the escrow will be applied to reduce the outstanding principal balance of the mortgage.

If the escrow is inadequate, or if additional items of repair are discovered at some subsequent date, it is the borrower's responsibility to bear the additional cost.

### **Calculating Maximum Mortgage with Repair Escrow**

The maximum mortgage amount and minimum cash investment must be calculated using form HUD-92900-LT.

### **HUD Forms**

For repair escrows, a completed "Mortgagee's Assurance of Completion," form HUD-92300, should be included in the case binder submitted for insurance endorsement and a completed "Compliance Inspection Report," form HUD-92051 must be submitted after completion of repairs.

Refer to: 4310.5 REV-2; Mortgagee Letter 95-56; Mortgagee Letter 00-27.

### **REO Appraisal Validity**

HUD obtains an appraisal to establish a list price for Real Estate Owned (REO) properties that are marketed for sale. If the buyer of the REO property is financing the purchase with an FHA loan, the Client must use the HUD appraisal as long as it is still valid. The validity period is 120 days. If a contract of sale is not ratified within 120 days of the appraisal, the lender must order a new appraisal or an appraisal update. The appraisal update must be performed by the original appraiser and the appraiser must make an exterior inspection of the subject property.

The appraiser must certify that the property has not declined in value based on research and analysis of current market data. The appraiser must also take pictures of the exterior of the property and certify that the property inspection does not reveal any deficiencies or significant changes since the original inspection.

With the exception of 203(k) as-repaired appraisals for REO properties, a second appraisal may not be ordered unless it is no longer valid as of the date the contract of sale was ratified, or if there are material deficiencies with the current appraisal. The DE underwriter is responsible for determining if there are material deficiencies. If a second appraisal is ordered, the DE underwriter must document the deficiencies and both appraisals must be retained in the case binder.

Refer to HUD REO Appraisal Validity Period and Second Appraisal Changes (ML 2010-08) for additional information.

### **Good Neighbor Next Door**

Revitalize neighborhoods by encouraging borrowers in selected professions to purchase and live in HUD-acquired single-family properties.

#### **Eligible borrowers**

Law enforcement officers

Firefighters

Emergency medical technicians (EMT s)

Private and public school teachers

If a married couple is eligible under more than one program, they are eligible to purchase under only one program.

Designated HUD-owned properties in revitalization/exception-criteria areas are eligible at 50% off the sale price as specified by HUD.

Loans must comply with FHA guidelines. The following program options are available:

#### **Eligible Properties**

Owner-occupied single family detached homes, PUDs and condos.

Borrowers must agree to occupy the property as a primary residence for three years without interruption.

**Note:** Under the GNND Sales Program, single-unit properties acquired by HUD located in HUD-designated revitalization areas (except occupied properties, those located in Asset Control Areas, or those that HUD has determined will be sold through an alternative sales method) will be available to interested law enforcement officers, teachers and firefighters/emergency medical technicians prior to listing the properties for sale to other purchasers.

### **Minimum Down Payment**

\$100

Closing cost and finance costs may be included in the mortgage amount up to a maximum of 100% LTV based on the current value.

### **Required Documents**

Certificate of Law Enforcement Officer, Teacher, Firefighter or EMT  
(HUD-9549-A)

Land Use Restrictions Addendum  
(HUD-9549-B)

Assignment of Sales Contract  
(HUD-9549-C)

Employer Verification of Participant Employment (HUD-9549-E)

For more info, visit the following HUD site:

<http://www.hud.gov/offices/hsg/sfh/reo/goodn/gnndabot.cfm>