



4900 Woodway Drive, Suite 650

Houston, TX 77056

Phone: 713-871-0005

Fax: 713-871-1358

Thomas E. Black, Jr., P. C.*

Calvin C. Mann, Jr., P. C.

Gregory S. Graham, P. C.

David F. Dulock

Diane M. Gleason

Benjamin R. Idziak **

Shawn P. Black **

Thomas L. Kapioltas

Margaret A. Noles

Robert J. Brewer

Marc E. Sanders ***

* Also Licensed in Iowa, New York,
Washington and West Virginia

** Also Licensed in New York

*** Licensed in New Mexico

July 2, 2008

To: Clients and Friends

From: David F. Dulock

Subject: FHA Implements Risk-based Premiums for Single Family Mortgage Insurance

In the May 13, 2008 *Federal Register*, FHA published notice that effective with new FHA case number assignments on or after July 14, 2008, it will implement risk-based premiums on one- to four-unit single family mortgages. Under these new requirements, FHA upfront and annual mortgage insurance premiums will be based on the prospective borrower's decision credit score in conjunction with the property's loan to value ratio. The *Federal Register* notice was followed by Mortgagee Letter 2008-16 issued June 11, 2008, that contains the risk-based premium matrixes and explains how to determine the borrower's decision credit score and the insured property's base LTV ratio, as well as additional practical information to assist FHA-approved lenders with risk-based premiums. A copy of Mortgagee Letter 2008-16 (ML 2008-16) is attached to this memorandum.

In summary, ML 2008-16 provides that:

1. The effective date is July 14, 2008, for FHA loans for which case numbers are assigned on or after that date.
2. There are two premium matrixes in ML 2008-16, one for loan terms greater than 15 years and the other for loan terms 15 years or less. These matrixes replace the premium matrix in [Mortgagee Letter 00-38](#), which identifies the current mortgage insurance premiums for FHA's single family programs.
3. FHA will make any subsequent changes to the risk-based premium matrixes in ML 2008-16 annually, to be effective at the beginning of FHA's fiscal year, which begins October 1 and ends September 30.
4. The premium matrixes are based solely on the prospective borrower's *decision credit score* and the *loan-to-value ratio* as defined in ML 2008-16.
5. For loan terms greater than 15 years, upfront mortgage insurance premiums (UFMIP) will range from 125 basis points to 225 basis points and annual premiums will either be 50 basis points or 55 basis points.
6. For loan terms 15 years or less, UFMIP will range from 100 basis points to 200 basis points and annual premiums will either be 0 basis points or 25 basis points.
7. No UFMIP will be greater than 225 basis points and no annual premium will be greater than 55 basis points.
8. Borrowers with credit bureau scores must be risk-classified by FHA's TOTAL (Technology Open to Approved Lenders) Mortgage Scorecard.
9. Borrowers without credit bureau scores must be manually underwritten and deemed as eligible based on criteria described in [Mortgagee Letter 2008-11](#); the mortgage insurance premium will be determined by the loan-to-value ratio for the "Non-traditional" column in the premium matrixes.
10. For loans involving multiple borrowers, the borrower representing the greatest risk will determine the UFMIP and annual premiums charged.
11. Those mortgage applicants in risk categories without a premium shown in the premium matrixes are not eligible for FHA-insured mortgage financing.

12. Certain first-time homebuyers who complete HUD-approved pre-purchase counseling will receive a reduction in UFMIP from 225 basis points to 200 basis points. Definitions and requirements are set out in ML 2008-16.
13. Except for streamline refinances, premiums are the same for purchase and refinance transactions (*i.e.*, based solely on the decision credit score in conjunction with the loan-to-value ratio).
14. There are no “add-ons” to the premiums or other adjustments to the mortgage insurance premiums for property type (*e.g.*, multiple unit properties and mortgages on manufactured housing).
15. The source of the downpayment is not a factor in determining the mortgage insurance premium.
16. Risk-based premium rates and the requirements of ML 2008-16 apply to forward mortgages insured under FHA’s MMIF (Mutual Mortgage Insurance Fund), the Section 203(k) rehabilitation mortgage insurance program, and individual condominium units insured under Section 234(c). Risk-based premium rates do not apply to: (i) mortgages insured under Title I of the National Housing Act, (ii) reverse mortgages under FHA’s Home Equity Conversion Mortgage (HECM) program, (iii) Section 223(e) (declining neighborhoods), (iv) Section 238(c) (military impact areas in Georgia and New York), (v) Section 247 (Hawaiian Homelands), and (vi) Section 248 (Indian Reservations).

Lender and third-party systems will need to be updated in order to calculate the appropriate risk-based UFMIP and annual mortgage insurance premiums required by FHA’s new policy expressed in the May 13, 2008 *Federal Register* notice and Mortgagee Letter 2008-16.

Please refer to the attached copy of Mortgagee Letter 2008-16 for a completion explanation of FHA’s policy regarding risk-based premiums for single family mortgage insurance.

<p>This Memorandum is provided for the general information of the clients and friends of our firm only and is not intended as specific legal advice. You should not place reliance on this general information alone but should consult legal counsel regarding the application of the information discussed in this Memorandum to your specific case or circumstances.</p>
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(Mortgagee Letter 2008-16 attached)

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

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

June 11, 2008

MORTGAGEE LETTER 2008-16

TO: ALL APPROVED MORTGAGEES

SUBJECT: Risk-Based Premiums for FHA Mortgage Insurance

Effective with new FHA case number assignments on or after July 14, 2008, FHA will implement risk-based premiums on one- to four-unit single family mortgages. The premium matrix is shown below, replacing the premium matrix in [Mortgagee Letter 00-38](#), which identifies the current mortgage insurance premiums for FHA's single family programs.

FHA Single Family Mortgage Insurance Upfront and Annual Mortgage Insurance Premiums (Loan Terms > 15 years) <i>Effective as of July 14, 2008</i>							
All premiums are specified in basis points (0.01%)							
Decision Credit Score (FICO)							
LTV	850-680	679-640	639-600	599-560	559-500	499-300	NON-TRADITIONAL
≤ 90.00	125/50	125/50	125/50	150/50	175/50	175/50	150/50
90.01-95.00	125/50	125/50	150/50	175/50	200/50	n/a	175/50
> 95	125/55	150/55	175/55	200/55	225 ^a /55	n/a	200/55

^a. A first-time homebuyer, with HUD-approved counseling, will pay only 200 basis points for the upfront mortgage insurance premiums.

The premium grid is based solely on the prospective borrower's credit bureau score and the loan-to-value ratio; both are defined below.

Future Changes to the Risk-based Premium Schedule

It is FHA's intent to make any subsequent changes to the risk-based premium schedule only on an annual basis and make them effective at the beginning of the fiscal year. FHA's fiscal year begins October 1 and ends September 30.

Highlights Regarding FHA's Risk-Based Premiums

- UFMIP will range from 1.25 percent of the loan amount for lower-risk borrowers to 2.25 percent for riskier borrowers.
- No borrower who qualifies for a FHA-insured mortgage will pay more than 2.25 percent on the upfront mortgage insurance premium (UFMIP) and 55 basis points for the annual premium.
- Borrowers with credit bureau scores must be risk-classified by FHA's TOTAL Mortgage Scorecard.
- Those in risk categories without a premium shown are not eligible for FHA-insured mortgage financing.
- Borrowers without credit bureau scores will need to be manually underwritten and deemed as eligible based on criteria described in [Mortgagee Letter 2008-11](#); the mortgage insurance premium will be determined by the loan-to-value ratio for the non-traditional column in the premium schedule.

Loan-to-Value

For risk-based premium purposes, the loan-to-value ratio, computed to two decimals (e.g., 95.65), is calculated by dividing the mortgage amount prior to adding on any upfront mortgage insurance premium by the sales price or appraised value, whichever is less. Please note that for purchase transactions, the loan-to-value will be the percentage of the sales price (or appraised value) that is borrowed, e.g., 97.75 percent, as prescribed by law. While borrowers must have at least a three percent cash investment into the property, a portion of their closing costs may be used to meet that amount.

For refinance transactions, which often include closing costs in the loan amount, the LTV is determined by dividing the loan amount prior to adding on any upfront mortgage insurance premium by the appraiser's estimate of value.

"Decision Credit Score" Defined

If a credit score is available, it must be used to determine the decision credit score for the application and the premium to be charged. A "decision credit score" is determined for each applicant according to the following rule: when three scores are available (one from each repository), the median (middle) value is used; when only two are available, the lesser of the two is chosen; when only one is available that score is used.

Multiple Borrowers. If more than one individual is applying for the same mortgage, the lender must determine the decision credit score for each individual borrower and then select the lower (or lowest if more than two borrowers). That "decision" credit score is then used to determine the appropriate insurance premium in conjunction with the LTV ratio.

Multiple Borrowers/One Without Credit Score(s). The borrower representing the greatest risk to the Department will determine the premium charged. For example, if the decision credit score for one borrower is between 559-500 and the other borrower is in the non-traditional credit category, the decision credit score between 559-500 is used to determine the premium. However, if the decision credit score for one borrower is between 639-600, and the other borrower is in the non-traditional credit category, the non-traditional credit category is used to determine the premium.

Multiple Borrowers/Ineligible Score. Borrowers who fall into a cell with no premium price shown are not eligible for FHA-insured financing. Lenders may consider reducing the loan-to-value ratio to 90 percent or removing the borrower from the loan to proceed with the application.

Borrower Disputes Credit Score. If the mortgage applicant(s) disputes the accuracy of the credit report and, thus, the credit scores:

- The borrower may delay the transaction and work to repair his/her credit, or
- The borrower may pay the mortgage insurance premium based on the credit score generated (and LTV)

Non-Traditional Credit

For premium purposes, the borrower representing the greatest risk to the Department will determine the premium to be charged (see Multiple Borrowers/One Without Credit Score(s)). For underwriting purposes, borrowers with non-traditional credit (or insufficient credit) must qualify based on the underwriting guidance described in [Mortgagee Letter 2008-11](#).

To clarify the guidance in [Mortgagee Letter 2008-11](#) regarding 'thin-file' credit reports, the intention was to give lenders the option to also use non-traditional credit sources should they have a minimum trade line requirement to use a credit bureau score. While the premium charged is based on the borrower representing the greatest risk to the Department, for underwriting purposes lenders may use non-traditional credit methodology to make their determination on the borrower's willingness to repay the new FHA-insured mortgage.

Refinancing Delinquent Loans into FHASecure

For borrowers refinancing **delinquent** non-FHA ARMs the Upfront mortgage insurance premiums (UFMIP) is set at **2.25** percent of the base loan amount (loan amount excluding UFMIP) regardless of the loan-to-value (LTV) ratio.

Automated underwriting systems will provide lenders with a feedback message that will inform them of the premium to be charged without recognizing that the loan being refinanced is delinquent. Therefore, the feedback message providing the premium message will caution lenders that if the loan being refinanced is delinquent, then the premium is **2.25** percent for the UFMIP and **.55** percent for annual premium when LTV ratio greater than 95 percent; if the LTV ratio is equal to or less than 95 percent, the annual premium is .50 percent.

Borrowers who refinance their delinquent non-FHA ARM loan into *FHASecure* and subsequently wish to refinance to another FHA-insured mortgage must use a refinance product that requires full qualifying, e.g., a rate and term refinance. Once the FHA-to-FHA full qualifying refinance is insured, these borrowers will be able to take advantage of FHA's Streamline Refinance program.

Underwriting Rules When Using FHA's TOTAL Mortgage Scorecard

If TOTAL renders a refer risk classification or triggers a review rule, the mortgagee's Direct Endorsement underwriter must determine whether the borrower qualifies for the mortgage using the basic underwriting and eligibility requirements outlined in [Mortgagee Letter 2004-47](#) (TOTAL Mortgage Scorecard User Guide) and handbook [HUD-4155.1 REV-5](#). However, once determined as eligible for a FHA-insured mortgage, the insurance premium charged is as shown in the matrix above.

Review Rules for FHA's TOTAL Mortgage Scorecard include excessive payment-to-income ratios and debt-to-income ratios; and from the credit files, a previous mortgage foreclosure within 3 years, a bankruptcy discharged within 2 years and late mortgage payments. TOTAL will refer the application for underwriting analysis if any mortgage trade line, including mortgage line-of-credit payments, during the most recent 12 months shows:

- 3 or more late payments of greater than 30 days; or
- 1 or more late payments of 60 days plus one or more 30-day late payments; or
- 1 payment greater than 90 days late

Although FHA will be charging a slightly higher mortgage insurance premium for certain categories of riskier transactions (e.g., borrowers with low credit bureau scores and high LTVs), those transactions referred by TOTAL are to be fully and properly underwritten. The increased premiums compensate FHA somewhat for the risk represented by the combination of LTV and credit bureau score, but are not themselves grounds for underwriter approval of a mortgage. The Refer decision from TOTAL suggests that, absent additional factors that can be documented by the underwriter, the credit risk of the loan may be too great for FHA to insure. Such mortgages, which may exhibit other risk-layering characteristics beyond credit bureau score and LTV, are to be approved solely on the underwriter's judgment of the likelihood of successful and sustained homeownership, not on the insurance premium collected.

If the underwriter approves a loan for which non-credit review rules are triggered, i.e., excessive payment-to-income ratios and debt-to-income ratios, the borrower will pay the mortgage insurance premium based on the decision credit score and LTV ratio.

First-Time Homebuyer with HUD-Approved Pre-Purchase Counseling

First-time homebuyers (as defined below) who will be obtaining a mortgage with an LTV greater than 95 percent and whose decision credit score is in the 559-500 range are entitled to a reduction of their upfront mortgage insurance premium from 2.25 percent to 2.00 percent provided the homebuyer completes HUD-approved pre-purchase counseling.

A first-time homebuyer is an individual who has had no ownership in a principal residence during the 3-year period ending on the date of purchase (closing date) of the property. A first-time homebuyer includes any individual that has only owned with a former spouse while married and also includes an individual who has only owned a principal residence not permanently affixed to a permanent foundation, or a property that was not in compliance with State, local, or model building codes and cannot be brought into compliance for less than the cost of constructing a permanent structure. If any of the occupant-owners on the mortgage meet this definition, then the mortgage is considered as having been made to a first-time homebuyer.

Pre-purchase counseling must be obtained from a HUD-approved housing counseling agency, a participating agency of a HUD-approved housing counseling intermediary or a state Housing Finance Agency receiving HUD housing counseling grant funds, and the counseling must occur prior to execution of the sales agreement. With this requirement, it is FHA's intent to encourage borrowers to participate in meaningful counseling prior to the decision to purchase a home, not to create an incentive or burden for lenders to have borrowers re-execute the sales contract in order to receive a reduced premium.

The counseling may be completed up to one year before the homebuyer signs a purchase agreement (executes a sales contract) for the subject property. It must be one-on-one, face-to-

face counseling unless a hardship can be demonstrated, and then the counseling may be conducted one-on-one over the telephone. The counseling must consist of, but is not limited to:

- Budgeting and credit, including an analysis of the household's unique financial/credit situation;
- Assessing homeownership readiness, including an evaluation of home and monthly payment affordability;
- Development of a written action plan outlining the steps the household and the counselor will take to help the household meet their goals;
- Financing a home, including a discussion of alternative types of mortgage loans/features and special financing products, common lending documents, and steps in the loan application, approval, and closing processes;
- Shopping for a home, including understanding the professionals involved in the process; and
- Maintaining a home, including preventive maintenance, taxes, and insurance

Even if group sessions or homebuyer education classes cover the topics above, they do not meet the level of one-on-one counseling needed to receive the reduced mortgage insurance premium. To find a list of housing counseling agencies, please visit the Department's website at <http://www.hud.gov/offices/hsg/sfh/hcc/hccprof14.cfm>.

Programs Covered by Risk-Based Premiums

Risk-based premiums and the requirements described in this mortgagee letter apply to those forward mortgages insured under FHA's Mutual Mortgage Insurance (MMI) fund, the Section 203(k) rehabilitation mortgage insurance program, and individual condominium units insured under Section 234(c). Risk-based premiums do not apply to mortgages insured under Title I of the National Housing Act, nor to reverse mortgages under FHA's Home Equity Conversion Mortgage (HECM). Risk-based premiums also do not apply to Section 223(e)(declining neighborhoods), Section 238(c)(Military Impact areas in Georgia and New York), Section 247 (Hawaiian Homelands), and Section 248 (Indian Reservations).

Refinance Transactions

The mortgage insurance premium for refinance transactions will depend on several variables. These include whether the refinance is of a FHA-insured mortgage to another FHA-insured mortgage, as under FHA's streamlined refinance options, is a rate-and-term refinance or is a refinance under the *FHASecure* initiative. Except for streamlined refinances and mortgage refinancing under the *FHASecure* initiative, the new LTV and new decision credit score determine the mortgage insurance premiums. Additional information is provided below:

Full Qualifying Refinances (e.g., rate-and-term; *FHASecure* refinance of a conventional mortgage not presently delinquent; cash-out refinances; any that require complete underwriting). These refinances are subject to the mortgage insurance premiums based on the LTV and decision credit score for the refinance application.

Streamline Refinances. The mortgage insurance premiums charged are subject to whether the existing FHA-insured loan being streamline refinanced was charged premiums based on A) the pre-July 14, 2008 premium structure of 150/50 basis points or B) the post July 14, 2008 LTV/decision credit score premium schedule. The following examples illustrate the appropriate premiums that will be charged for streamline refinances.

A. FHA-insured loans pre-July 14, 2008/Borrower paid 150/50 basis points

- Borrowers with an existing FHA-insured loan where the case number for the streamline refinance transaction was assigned before July 14, 2008, will be charged 150 basis points upfront and 50 basis points annually. On subsequent streamline refinances where the case number is assigned on or after July 14, 2008 borrowers will be charged 100 basis points upfront and 50 basis points annually.
- Borrowers with an existing FHA-insured mortgage where the case number for the streamline refinance transaction was assigned on or after July 14, 2008, will be charged 100 basis points upfront and 50 basis points annually. On subsequent streamline refinances borrowers will be charged 100 basis points upfront and 50 basis points annually.

B. FHA-insured loans On or After July 14, 2008/Borrower paid Risk-based Premium

- Borrowers with an existing FHA-insured mortgage (purchase or full qualifying refinance transaction) where the case number for that existing mortgage was assigned on or after July 14, 2008, will be charged premiums on the subsequent streamline refinance transaction using the decision credit score and LTV for the existing mortgage being refinanced.
- If the streamline refinance transaction is “credit qualifying” (with or without an appraisal) premiums are based on the new decision credit score and the LTV from the existing mortgage being refinanced.

Borrowers who refinanced their delinquent non-FHA ARM into an *FHASecure* mortgage are not eligible to streamline refinance their *FHASecure* mortgage. The refinance transaction subsequent to the *FHASecure* mortgage must be a full qualifying refinance.

Previous Case Number. To determine the case number of the loan being refinanced, lenders may use the Case Query screen in FHA Connection using the borrower’s name, address and/or social security number.

Premium Feedback. The Case Number Assignment screen in FHA Connection will provide a feedback message with the appropriate premium to be charged for refinance transactions.

Refund of Upfront Premiums. Refunds of upfront premiums are available to borrowers refinancing to another FHA-insured mortgage within a three-year time period, as shown below.

Upfront Mortgage Insurance Premium Refund Percentages												
	Month of Year											
Year	1	2	3	4	5	6	7	8	9	10	11	12
1	80	78	76	74	72	70	68	66	64	62	60	58
2	56	54	52	50	48	46	44	42	40	38	36	34
3	32	30	28	26	24	22	20	18	16	14	12	10

On any refinance where the MIP refund exceeds the Upfront MIP required on the new loan, the overage will be refunded directly to the borrower from HUD. The lesser of the MIP refund or the new upfront MIP should be subtracted from the unpaid principal balance before calculating the new mortgage amount.

Type of Refinance	Risk-Based Premium Information
Cash-Out Refinances	Premiums based on new LTV and credit bureau score/see premium matrix
Rate-and-Term Refinance (no cash out)	Premiums based on new LTV and credit bureau score/see premium matrix
FHA Secure/Not Delinquent	Premiums based on new LTV and credit bureau score/see premium matrix
FHA Secure/Delinquent	Premium is 2.25% upfront. Annual premium is 55 basis points if LTV > 95%; otherwise, 50 basis points
Streamlined Refinance of RBP Loan	Premiums based on previous LTV and previous credit bureau score/FHA will provide feedback with initial values/Any refund to be applied to new upfront premium
“Credit qualifying” Streamlined Refinance	Premiums based on new credit bureau score and previous LTV/FHA will provide feedback with initial values/ Any refund to be applied to new upfront premium
Streamline Refinance with new case number assigned prior to July 14, 2008	Premium is 1.50 percent upfront and .50 percent annually/ Any refund to be applied to new upfront premium
Streamline Refinance with new case number assigned on or after July 14, 2008	Premium is 1.00 percent upfront and .50 percent annually/ Any refund to be applied to new upfront premium

15 Year and Shorter-Term Mortgages

Mortgages with terms of 15 years or fewer have a slightly different upfront and annual premium structure due to the risk shorter-term mortgages represent. The mortgage insurance premium matrix is shown below:

FHA Single Family Mortgage Insurance Upfront Mortgage and Annual Mortgage Insurance Premiums Loan Terms of 15 Years or Fewer <i>Effective as of July 14, 2008</i>							
All premiums are specified in basis points (0.01%)							
Decision Credit Score (FICO)							
LTV	850-680	679-640	639-600	599-560	559-500	499-300	NON-TRADITIONAL
≤ 90.00	100/0	100/0	125/0	150/0	175/0	175/0	150/0
90.01-95.00	100/25	125/25	150/25	175/25	200/25	n/a	175/25
> 95	125/25	150/25	175/25	200/25	200/25	n/a	200/25

Systems

Lenders are reminded of the importance of data integrity to ensure that the appropriate premium is charged and that the data submitted to TOTAL and FHA Connection is accurate. Also, system edits will prevent lenders from Streamline Refinancing FHASecure loans that were previously delinquent non-FHA ARM loans.

Additional Information about FHA's Risk-Based Premiums

- Except for streamline refinances, premiums are the same for purchase and refinance transactions, i.e., based solely on the decision credit bureau score and the loan-to-value ratio
- There are no "add-ons" to the premiums or other adjustments to the mortgage insurance premiums for property type, e.g., multiple unit properties and mortgages on manufactured housing
- The source of the downpayment is not a factor in determining the mortgage insurance premium

If you should have any questions concerning this Mortgagee Letter, call 1-800-CALLFHA.

Sincerely,

Brian D. Montgomery
Assistant Secretary for Housing-
Federal Housing Commissioner