Options for FHA-Insured Mortgages


HUD-funded foreclosure prevention counseling can be obtained from your HUD regional office or you can call 800-569-4287 (TDD 800-877-8339) or go on www.hud.gov [3] to find HUD-approved counselors. Check a counseling agency’s website to see if it provides foreclosure prevention counseling.

If you experience difficulties with a servicer who is not following FHA guidelines, you can seek help through the FHA National Servicing Center (NSC). Mail Department of Housing and Urban Development, National Servicing Center, 301 N.W. 6th St., Suite 200, Oklahoma City, OK 73201 or call 888-297-8685. Be sure to send your servicer a copy of any letter you send to the NSC.

Servicer Initial Obligations When You Are Delinquent. Servicers will send you notice of your default of an FHA mortgage which explains what you need to do to get your loan reinstated. Servicers must also make reasonable efforts to arrange a face-to-face interview with you before three full monthly installments are overdue. The servicer may not initiate foreclosure until it has considered whether you qualify for one of the loss mitigation options discussed below.

Before You Get to the FHA-HAMP Program. While FHA-HAMP can reduce your monthly loan payment, some borrowers are not eligible for FHA-HAMP—they only qualify for a repayment plan or a forbearance agreement, which do not permanently change the basic terms of their loans. In a repayment plan, each month you make your normal monthly payment plus pay a portion of your delinquent payments on top of that. The plan gives you the opportunity to get caught up on your back-due payments over a period of months. A forbearance agreement does not excuse you from eventually making all your payments, but does allow you for a period of months to reduce or skip your payments.

There are three basic situations where you will only be offered a repayment plan or a forbearance agreement instead of the FHA-HAMP program:

1. If you have not experienced a verified loss of income or increase in living expenses, the servicer must offer you a short-term repayment plan or forbearance agreement. If the plan is going to extend for longer than three months, it must be in writing; shorter plans can be provided orally. The plans cannot extend longer than six months, unless HUD authorizes the extension.

2. You do not have “continuous income” that is reasonably likely to continue through at least the next twelve months. Continuous income includes employment income, pensions, Social Security, disability, veterans’ benefits, and child support payments. FHA’s option for borrowers without continuous income is a special forbearance plan that reduces or suspends your payments for a fixed time or until you begin to receive continuous income, up to a maximum of one year. At the end of the forbearance period the servicer must evaluate you for the full range of FHA loss mitigation options.

3. If you have too much income, you can be forced into a repayment agreement of up to six months. This happens if you have sufficient net income left after you pay your normal monthly living expenses and your recurring monthly debt, so that you can handle a repayment agreement that will bring you current within six months. In addition, if your current total mortgage payments take up less than 31% of your gross income, you may have to provide additional documentation about your income and expenses.

Who Qualifies for the FHA-HAMP Program. Unless you are excluded by one of the threshold tests described above, your servicer must evaluate you for FHA-HAMP which can permanently reduce your monthly payments. FHA-HAMP uses a complicated formula set out below to determine your loan modification, based on your income and loan payment. Once this loan modification is determined, you will be on a three-month trial plan on reduced payments. If that goes well, you will receive a permanent modification with lower mortgage payments.

To qualify for the FHA-HAMP program, the property must be owner-occupied. The borrowers must be in default or at imminent risk of default. Borrowers who have received a chapter 7 bankruptcy discharge and did not reaffirm their mortgage debt are eligible for FHA-HAMP, as are borrowers currently in bankruptcy. A default on an FHA-HAMP trial modification does not preclude later eligibility for a new modification, so long as the borrower can demonstrate changed circumstances justifying the new application. Borrowers are limited to one permanent FHA-HAMP modification in a two-year period.
Calculating Your FHA-HAMP Loan Modification. The first step in determining your FHA-HAMP loan modification is to calculate a monthly payment that FHA thinks you can afford, called the “target payment amount.” Select the greater of 80% of your current monthly payment (including escrow) with 25% of your gross monthly income. The target payment is the lesser of that resulting number and 31% of your gross monthly income.

The next step initially calculates a proposed modification. The total amount of outstanding unpaid interest, advances, and legitimate foreclosure fees and costs are added to the existing principal balance to form a new modified principal balance. This new balance is amortized over a 360-month term running from the modification date. A new fixed interest rate is set at a current market rate. These calculations generate a new monthly payment, which is added to the current monthly escrow payment to produce an estimated total monthly modified payment.

If this initial modification calculation produces a number at or below the “target payment amount,” the servicer should offer you a modification with those fixed terms. If it produces a number higher than the “target payment amount,” then FHA determines that you need more help. Your servicer must then reduce the principal balance to which the new interest rate and 360-month term is applied to reach a lower monthly payment for you. With one exception discussed below, the principal balance is reduced enough so that your payment gets down to the target monthly payment. FHA calls the amount of the principal balance that is reduced a “partial claim.”

A partial claim does not eliminate your obligation to pay the amount reduced from your principal balance, but instead is an interest-free loan, secured by a secondary lien on your home. You do not have to pay this loan off until you pay off your FHA first mortgage or stop living in the home. The FHA-HAMP program can provide you with as large a partial claim as you will need to bring your payments down to a “target payment,” but the total amount that can be included in all partial claims FHA can offer you during your mortgage is limited to 30% of the unpaid principal balance owed at the time of your initial partial claim.

If the cap is reached, your payment is lowered as far as possible until the partial claim cap is reached, as long as your total modified monthly payment is lower than 40% of your gross monthly income. If your payment would be higher than 40% of your gross income, you should be considered for special forbearance or an option involving loss of your home.

Short Sales and Deeds in Lieu of Foreclosure. FHA provides for a short sale, letting you sell your home and use the proceeds to satisfy your mortgage even if the proceeds are less than the amount you owe on the loan. The FHA limits approvals of short sales based on the ratio of the property’s value to the outstanding debt and on the ratio between the short sale purchase price and the property’s value. To qualify for an FHA short sale you must document financial hardship. No documentation is needed if you occupy the property, are ninety days or more delinquent, and have a credit score below 620. You must be able to sell your home within four months of your approval. This period may be extended for two more months if you have a signed purchase and sale agreement or if your lender qualifies under certain program rules. The sale proceeds must pay off any liens that are junior to the FHA mortgage. The FHA will provide you with an incentive payment of up to $3,000 when you complete the short sale.

FHA offers a “deed in lieu of foreclosure” option that lets you transfer your home voluntarily to the FHA in exchange for a release from all your obligations under the mortgage. You must submit verification of hardship, and a complete application with calculation of your cash reserves. You can avoid this documentation requirement if you occupy the property, are ninety days or more delinquent, and have a credit score below 620. The FHA will generally not accept a “deed in lieu” if you have a tenant. Instead you must first attempt to sell your home through a short sale.

The FHA pays you $2,000 for completing a deed in lieu. However, if there are any other liens on the property, the payment may be used to help pay off those liens. The deed in lieu option will not be approved unless all junior liens can be paid off with the transfer.

A short sale and a deed in lieu of foreclosure can have tax implications. For more on both these tax implications and for other useful information about short sales and deeds in lieu, refer to the discussion above in this chapter concerning Fannie Mae and Freddie Mac short sales and deeds in lieu.
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