Section B. ARMS

Overview

In This Section

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</tr>
</tbody>
</table>
1. Terms and Definitions for Adjustable Rate Mortgages (ARMs)

Change Date

March 24, 2011

4155.1 6.B.1.a Locating Terms and Definitions Related to ARMs

See HUD 4155.1 9.1 for definitions of the following terms related to Adjustable Rate Mortgages (ARMs):

- adjusted interest rate
- calculated interest rate
- change date
- current index
- existing interest rate
- initial interest rate
- index, and
- margin.
2. General Information on ARMs

Introduction
This topic contains general information on ARMs, including

- ARM interest rate adjustments and caps
- hybrid ARM program eligibility
- the maximum number of ARM units insured by FHA, and
- ARM loan features.

Change Date
March 24, 2011

4155.1 6.B.2.a
ARM Interest Rate Adjustments and Caps

The table below describes the annual interest rate adjustment and interest rate cap over the life of the five types of Adjustable Rate Mortgage (ARM) loans.

Reference: For more information on the frequency of interest rate changes, see HUD 4155.1 6.B.4.e.

<table>
<thead>
<tr>
<th>When the ARM is initially at a fixed interest rate for ...</th>
<th>Then the annual interest rate adjustment, after the initial fixed interest rate period, is ...</th>
<th>And the interest rate cap over the life of the loan is ...</th>
</tr>
</thead>
<tbody>
<tr>
<td>• 1 year</td>
<td>one percentage point</td>
<td>five percentage points.</td>
</tr>
<tr>
<td>• 3 years, or</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• 5 years</td>
<td>two percentage points</td>
<td>six percentage points.</td>
</tr>
<tr>
<td>• 5 years</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• 7 years, or</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• 10 years</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: FHA added the two options for the five-year ARM in order to meet the needs of borrowers, lenders and the secondary mortgage market.

Continued on next page
2. General Information on ARMs, Continued

4155.1 6.B.2.b Hybrid ARM Program Eligibility

Owner-occupied principal residences being insured under the following programs are eligible for hybrid ARMs:

- Section 203(b), Home Mortgage Insurance Program
- Section 203(h), Home Mortgage Insurance for Disaster Victims Program
- 203(k), Rehabilitation Home Mortgage Insurance Program, and
- 234(c), Mortgage Insurance for Condominium Units.

Nonprofits, including organizations normally eligible as borrowers, and government agencies are not permitted to apply for the hybrid ARM products.

References: For information on Section 203 mortgage insurance programs, see

- HUD 4155.1 6.A.6, and
- HUD 4155.2 1.C.

4155.1 6.B.2.c Maximum Number of ARM Units Insured

The aggregate number of all ARMs insured by FHA in any fiscal year may not exceed 30% of the aggregate number of mortgages insured during the preceding fiscal year.

FHA will notify lenders when the maximum percentage is close to being reached during any fiscal year.

4155.1 6.B.2.d ARM Loan Features

The lender and borrower negotiate the initial interest rate and margin. The margin must be constant for the entire term of the mortgage.

The interest rate remains constant for the initial period (either a 1, 3, 5, 7, or 10 year period, depending on the ARM) and then may change annually for the remainder of the loan term.
3. ARM Underwriting Requirements

**Introduction**

This topic contains information on underwriting ARMs, including

- ARM underwriting requirements
- ARM application disclosure
- annual MIP on an ARM
- ARM mortgage document requirements
- borrower qualifying on the 1-year ARM
- borrower qualifying on the 3, 5, 7, or 10 year ARM
- temporary interest rate buydowns on ARMs
- ARM loan maturity
- model ARM Note, and
- ARM amortization provisions.

**Change Date**

March 24, 2011

**4155.1 6.B.3.a ARM Underwriting Requirements**

Adjustable Rate Mortgage (ARM) loans must be processed and underwritten using the initial interest rate negotiated between the lender and borrower as stated on Form HUD 92900-A, *Addendum to Uniform Residential Loan Application*.

Mortgage credit processing must be in accordance with existing FHA instructions, except as modified subsequently in this topic.

**References**: For more information on calculating qualifying ratios on a

- 1 year ARM, see HUD 4155.1 6.B.3.e, and
- 3, 5, 7 or 10 year ARM, see HUD 4155.1 6.B.3.f.

*Continued on next page*
3. **ARM Underwriting Requirements**, Continued

4155.1 6.B.3.b

ARM Application Disclosure

When the borrower applies for an ARM loan, the lender must provide him/her with a written explanation of the

- nature of the proposed obligation, and
- features of an ARM, consistent with the disclosure requirements applicable to variable-rate mortgages secured by a principal dwelling under the Truth-in-Lending Act (TILA), “Regulation Z” at
  - 15 United States Code (USC) 1601, and

Additionally, the lender must provide the borrower with a hypothetical monthly payment schedule that displays the maximum potential increases in monthly payments for the term of the ARM. The hypothetical payment schedule should illustrate the maximum increases over the shortest possible time frame.

*Example*: A 7 year ARM payment schedule should show the maximum potential increases over the three years following the initial fixed interest rate period of seven years.

Notes:
- FHA relies on lenders to comply with TILA, and does not provide disclosures for the ARM products.
- The ARM disclosure statement, signed by all borrowers, must accompany the loan application and applicable FHA addenda.

4155.1 6.B.3.c

Annual MIP on an ARM

The annual mortgage insurance premium (MIP) amount and any termination provisions must be based on the initial interest rate throughout the term of the loan, regardless of the interest rate adjustments to the loan.

4155.1 6.B.3.d

ARM Mortgage Document Requirements

The mortgage documents for an ARM must specify the

- initial interest rate
- margin
- date of the first adjustment to the interest rate, and
- frequency of adjustments.

*Continued on next page*
## 3. ARM Underwriting Requirements, Continued

<table>
<thead>
<tr>
<th><strong>4155.1 6.B.3.e</strong></th>
<th>Borrower Qualifying on the 1 Year ARM</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>4155.1 6.B.3.e</strong></td>
<td>Borrowers choosing the 1 year ARM where the loan-to-value (LTV) is 95% percent or greater, must qualify for payments based on the contract or initial rate plus 1.0%.</td>
</tr>
<tr>
<td><strong>For this purpose, the LTV is defined as the lesser of the</strong></td>
<td></td>
</tr>
<tr>
<td>• base loan amount divided by the appraiser’s estimate of value, or</td>
<td></td>
</tr>
<tr>
<td>• percentage shown on the “LTV” line under the Qualifying Ratios section on the HUD-92900-LT.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>4155.1 6.B.3.f</strong></th>
<th>Borrower Qualifying on the 3, 5, 7, or 10 Year ARM</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>4155.1 6.B.3.f</strong></td>
<td>Borrowers choosing the 3, 5, 7, or 10 year ARMs must qualify for payments based on the entry level or Note rate. These ARMs do not require underwriting at one percentage point above the note rate.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>4155.1 6.B.3.g</strong></th>
<th>Temporary Interest Rate Buydowns on ARMs</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>4155.1 6.B.3.g</strong></td>
<td>Any form of temporary interest rate buydown is prohibited for all ARMs, regardless of LTV. If there is a permanent buydown, underwriting must be based on the rate in the application.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>4155.1 6.B.3.h</strong></th>
<th>ARM Loan Maturity</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>4155.1 6.B.3.h</strong></td>
<td>ARM loan maturities shall not exceed 30 years.</td>
</tr>
</tbody>
</table>

*Continued on next page*
3. **ARM Underwriting Requirements**, Continued

<table>
<thead>
<tr>
<th>4155.1 6.B.3.i</th>
<th>Model ARM Note</th>
<th>Lenders must modify the model <a href="#">ARM Note</a> form found in <strong>HUD 4155.2 12.A.4.a</strong> to accommodate the type of ARM being offered, including the</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>• Change Date</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• limits on the interest rate changes associated with the initial fixed rate period of the ARM, and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• lifetime caps.</td>
</tr>
<tr>
<td>Note:</td>
<td>Existing model notes and security instruments currently reflect only the 1 Year <a href="#">CMT Index</a>. Therefore, when <a href="#">LIBOR</a> rates are chosen, the Adjustable Rate notes and other related documents must reflect the applicable LIBOR index.</td>
<td></td>
</tr>
<tr>
<td>Reference:</td>
<td>For information on the model ARM Note, see <a href="#">HUD 4155.2 6.B</a>.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>4155.1 6.B.3.j</th>
<th>ARM Amortization Provisions</th>
<th>The <a href="#">ARM must</a></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>• be fully-amortizing, and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• contain amortization provisions that allow for periodic adjustments in the rate of interest charged.</td>
</tr>
</tbody>
</table>
4. Interest Rate Index

Introduction

This topic contains information on the ARM interest rate index, including:

- acceptable ARM indices
- ARM index information
- adjusting the interest rate on an ARM
- use of margin to adjust interest rate on ARM, and
- frequency of interest rate changes on ARMs.

Change Date

March 24, 2011

4155.1 6.B.4.a
Acceptable
ARM Indices

FHA will insure forward Adjustable Rate Mortgage (ARM) loan products using either the:

- 1 Year London Interbank Offered Rate (LIBOR), or
- 1 Year Constant Maturity Treasury (CMT) index.

Notes:
- The two index types cannot be commingled.
- Either index may be used for 1, 3, 5, 7, or 10 year ARMs.

Reference: For more information on the indices, see HUD 4155.1 6.B.4.b.
4. Interest Rate Index, Continued

Upward or downward changes in the interest rate charged on an ARM, except as otherwise provided in this section, must correspond to changes in the index, either the

- 1 Year CMT, defined as the weekly average yield on United States (U.S.) Treasury securities adjusted to a constant maturity of one year, or equivalent, as
  – provided by the Department of the Treasury, and
  – found on the Federal Reserve Statistical Release H.15, Selected Interest Rates website at www.federalreserve.gov/releases, or
- 1 Year LIBOR index as published in the Wall Street Journal.

Notes:
- The Federal Reserve Statistical Release is published weekly on Monday, or on Tuesday if Monday is a Federal holiday.
- The LIBOR indices are published in the Wall Street Journal on the first business day of each week, typically a Monday, or Tuesday if Monday is a non-publishing day.
- Should the Federal Reserve begin publishing the LIBOR indices in H.15, then lenders must use the H.15 as the source for LIBOR rates.
- The LIBOR indices are effective from the day they are published, until the day they are published the following week.
- The published LIBOR index must be rounded to three digits to the right of the decimal point.

Continued on next page
4. Interest Rate Index, Continued

Establishing the Adjusted Interest Rate on an ARM

When establishing the adjusted interest rate on an ARM, the servicer must compare the initial contract interest rate to the sum of the current index figure and the mortgage margin (calculated interest rate).

The adjusted interest rate will be the interest rate charged to the borrower, subject to the limitations of the annual and lifetime caps for the respective ARM type.

The current index figure must be the most recent index figure available 30 calendar days before the Change Date (the effective date of an adjustment to the interest rate, as shown in Paragraph 5(a) of the model Adjustable Rate Note form.)

Use of Margin to Adjust Interest Rate on ARM

Section 203.49 (c) of the regulations provides an alternative method to using the margin to set the new interest rate on an ARM, stating that to set the new interest rate, the lender will

- determine the change between the initial or base index figure, and the current index figure, or
- add a specified margin to the current index figure.

Ginnie Mae will only purchase ARMs that use the margin method for establishing the new interest rate. HUD requests that the lender contact the FHA Single Family Program Development Office for guidance if it wishes to use the other method for establishing the new interest rate.

Continued on next page
4. **Interest Rate Index**, Continued

Interest rate adjustments must occur on an annual basis, after the first adjustment.

The table below describes exceptions for the first adjustment rate change date.

<table>
<thead>
<tr>
<th>If the ARM is initially at a fixed interest rate for ...</th>
<th>Then the first adjustment rate change may occur no sooner than ...</th>
<th>And no later than ...</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 year</td>
<td>12 months</td>
<td>18 months.</td>
</tr>
<tr>
<td>3 years</td>
<td>36 months</td>
<td>42 months.</td>
</tr>
<tr>
<td>5 years</td>
<td>60 months</td>
<td>66 months.</td>
</tr>
<tr>
<td>7 years</td>
<td>84 months</td>
<td>90 months.</td>
</tr>
<tr>
<td>10 years</td>
<td>120 months</td>
<td>126 months.</td>
</tr>
</tbody>
</table>
5. Calculating Interest Rate Adjustments on ARMs

Introduction

This topic contains information on how to calculate interest rate adjustments on ARMs, including

- calculating annual adjustments
- current basis for the index
- determining the current index figures
- determining the calculated interest rate
- determining the new adjusted interest rate
- interest rate adjustments over the term of the mortgage, and
- effective date for the adjusted interest rate.

Change Date

March 24, 2011

4155.1 6.B.5.a Calculating Annual Adjustments on ARMs

To calculate the annual adjustments to the initial interest rate on an adjustable rate mortgage (ARM), the lender must

- determine the current index (London Interbank Offered Rate (LIBOR), or Constant Maturity Treasury (CMT))
- determine the calculated interest rate, and
- compare the calculated interest rate to the existing interest rate to determine the new adjusted interest rate subject to the annual and lifetime caps.

Note: Once the new adjusted interest rate is calculated, notice of the change must be provided to the borrower.

References: For information on

- determining the current index, see HUD 4155.1 6.B.5.c
- determining the calculated interest rate, see HUD 4155.1 6.B.5.d
- comparing the calculated interest rate to the existing interest rate to determine the new adjusted interest rate, see HUD 4155.1 6.B.5.e, and
- providing notice to the borrower of the interest rate change, see HUD 4155.1 6.B.7.

Continued on next page
5. Calculating Interest Rate Adjustments on ARMs, Continued

4155.1 6.B.5.b
Basis for the ARM Index

The ARM index used is based on either the
- weekly LIBOR rate, or
- weekly average yield on U.S. Treasury securities, adjusted to a constant maturity of one year (CMT).

The index used must be
- the one effective on the date 30 calendar days before the Change Date, and
- either the
  – CMT, shown on the Federal Reserve Board Statistical Release H.15 (effective the day it is issued, until a new H.15 index is published), or
  – LIBOR, shown in the Wall Street Journal (effective the day it is issued, until a new weekly Wall Street Journal is published).

4155.1 6.B.5.c
Determining the Current Index Figure on an ARM

The table below describes the current index figure to use based upon the particular day of the week on which the 30th calendar day falls. See HUD 4155.1 6.B.5.b for a description of the two indices and where they are published.

<table>
<thead>
<tr>
<th>When the 30th calendar day falls on a ...</th>
<th>Then use the index figure issued on ...</th>
<th>If the 30th calendar day prior to a Change Date...</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monday that is a business day</td>
<td>that Monday</td>
<td>and the issue date of an H.15 release both occur on the same day (that is, they both occur on a Monday).</td>
</tr>
<tr>
<td>Monday that is a Federal holiday</td>
<td>the prior week</td>
<td>falls on a Monday that is a Federal holiday.</td>
</tr>
</tbody>
</table>

Continued on next page
5. Calculating Interest Rate Adjustments on ARMs, Continued

4155.1 6.B.5.c Determining the Current Index Figure on an ARM (continued)

<table>
<thead>
<tr>
<th>When the 30th calendar day falls on a day of the week other than Monday</th>
<th>Then use the index figure issued on the Monday of that week (or issued on Tuesday if that Monday is a Federal holiday.)</th>
<th>If …</th>
</tr>
</thead>
</table>

*Example:* Assuming a Change Date of December 1, 2005, 30 calendar days before December 1 is Tuesday, November 1. Use the correct index figure issued on Monday, October 31.

---

4155.1 6.B.5.d Determining the Calculated Interest Rate on an ARM

The calculated interest rate is the current index, plus the margin (the number of basis points identified as “margin” in Paragraph 5(C) of the model Adjustable Rate Note), rounded to the nearest 1/8th of one percentage point (0.125 percent).

This complies with Ginnie Mae’s requirement that mortgages placed into Ginnie Mae pools must be rounded to the nearest 1/8th of one percentage point at each Change Date.
5. Calculating Interest Rate Adjustments on ARMs, Continued

4155.1 6.B.5.e Determining the New Adjusted Interest Rate on an ARM

Compare the calculated interest rate to the existing interest rate in effect for the preceding 12 months, to determine the new adjusted interest rate.

The table below provides instructions on determining the new adjusted interest rate, based upon the results of the comparison between the

- calculated interest rate, and
- existing interest rate.

<table>
<thead>
<tr>
<th>If the calculated interest rate is ...</th>
<th>Then the new adjusted rate will be ...</th>
</tr>
</thead>
<tbody>
<tr>
<td>equal to the existing interest rate</td>
<td>the same as the existing interest rate.</td>
</tr>
</tbody>
</table>
| less than the existing interest rate   | • the calculated interest rate, for one-three- and five-year ARMs if the calculated interest rate is less than one percentage point higher or lower than the existing interest rate, and  
                                          • the calculated interest rate for five, seven- and ten-year ARMs if the calculated interest rate is less than two percentage points higher or lower than the existing interest rate. |
| more than the existing interest rate   | • limited to one percentage point higher or lower than the existing interest rate for one, three, and five year ARMs, if the new calculated interest rate is more than one percentage point (100 basis points) higher or lower than the existing interest rate. (Note: Index changes in excess of one percentage point may not be carried over for inclusion in an adjustment in a subsequent year.), and  
                                          • the calculated interest rate for five, seven and ten year ARMs, if the calculated interest rate is more than two percentage points (200 basis points) higher or lower than the existing interest rate. (Note: Index changes in excess of two percentage points may not be carried over for inclusion in an adjustment in a subsequent year.) |

Continued on next page
5. Calculating Interest Rate Adjustments on ARMs, Continued

Adjustments to the interest rate over the entire term of the mortgage may not result in a change in either direction of more than

- five percentage points (500 basis points) from the initial contract interest rate for one, three, and five year ARMs, or
- six percentage points (600 basis points) for five, seven and ten year ARMs.

An adjusted interest rate is effective on the Change Date, and thereafter is deemed to be the existing interest rate. The new rate remains in effect until the next Change Date.

During the term of the mortgage, each adjustment is effective on the same date of each succeeding year.
6. Computing the Monthly Installment Payment on an ARM

Introduction
This topic contains information on the monthly installment payment after an ARM adjustment, including

- determining the new monthly payment, and
- the timing of the new monthly payment.

Change Date
March 24, 2011

4155.1 6.B.6.a
Determining New Monthly Payment After ARM Adjustment

Interest rate changes may only be implemented through adjustments to the borrower’s monthly payments. The lender must determine a new monthly payment each time there is an interest rate adjustment, as described in HUD 4155.1 6.B.5.

The portion of the monthly payment attributable to principal and interest is calculated by

- determining the amount necessary to fully amortize the unpaid principal balance for the remaining term of the mortgage
- crediting all eligible prepayments, and
- not debiting any delinquency.

Notes:
- The unpaid principal balance for to calculate the monthly installment is the balance that would be due on the Change Date if there had been no default in any payment, but reduced by the amount of any prepayments made to the principal.
- All ARM adjustments affect interest rates only. Negative amortization is not permitted.

Continued on next page
Since interest is payable on the first day of the month following the month in which the interest accrued, the borrower will begin to pay the new monthly payment 30 days after the Change Date, provided the lender gives the borrower proper notice.

**Reference:** For information on the requirements for Annual ARM Adjustment Notices to the borrower, see HUD 4155.1 6.B.7 and HUD 4155.1 6.B.8.
7. Annual ARM Adjustment Notice Requirements

Introduction
This topic contains information regarding the Annual Adjustment Notice, including:

- annual ARM Adjustment Notice policy
- required ARM Notice content
- sending the ARM Adjustment Notice
- lender ARM notification obligation during foreclosure and delinquency
- annual ARM Adjustment Notice record retention, and
- collection action after ARM adjustment.

Change Date
March 24, 2011

4155.1 6.B.7.a Annual ARM Adjustment Notice Policy
At least 25 days before any adjustment to a borrower’s monthly payment may occur, the lender must provide written notification regarding:

- the new mortgage interest rate
- the amount of the new monthly payment
- the current index, and
- how the payment adjustment was calculated.

Prior to issuance of the notice, the lender must calculate the new adjusted interest rate, as instructed in HUD 4155.1 6.B.5.

The first adjustment to the interest rate becomes effective on the date specified in Paragraph 5A (Change Date) of the Adjustable Rate Mortgage Model Note and thereafter, each adjustment becomes effective on the same date of each succeeding year during the term of the mortgage.

Note: Lenders must notify borrowers
- 30 days before any adjustments, if this provision is stated in the mortgage agreement, and
- annually, even if the existing interest rate does not change.

Continued on next page
7. Annual ARM Adjustment Notice Requirements, Continued

4155.1 6.B.7.b Required ARM Notice Content

The content of the Adjustment Notice must meet the criteria of 24 CFR 203.49(h), Eligibility of Adjustable Rate Mortgages, and include the

- date the Adjustment Notice is mailed
- change date
- existing interest rate
- adjusted interest rate
- current Index and publishing date
- method of calculating the adjustment to monthly payments
- amount of the adjusted monthly payments, and
- any other information that may be required by law, such as an explanation of why the adjusted interest rate is less than the calculated interest rate when the cap is reached.

4155.1 6.B.7.c Sending the ARM Adjustment Notice

The lender should send the Adjustment Notice to the borrower by Certified Mail, Return Receipt Requested.

The lender can also send the Notice by first class mail to all property owners identified on its records, unless the borrower’s whereabouts are known to be elsewhere.

4155.1 6.B.7.d Lender ARM Notification Obligation During Foreclosure or Delinquency

The lender’s obligation to compute and adjust the interest rate and provide notice to the borrower is not affected by delinquencies or foreclosures, so long as the mortgage debt exists.

It is the lender’s responsibility to see that its collection actions continually update the mortgage debt.

Continued on next page
### 7. Annual ARM Adjustment Notice Requirements, Continued

<table>
<thead>
<tr>
<th>4155.1 6.B.7.e Annual ARM Adjustment Notice Record Retention</th>
</tr>
</thead>
<tbody>
<tr>
<td>For HUD review purposes, lenders must</td>
</tr>
<tr>
<td>- keep evidence that timely notice was sent to the borrower, and</td>
</tr>
<tr>
<td>- retain annual adjustment computations for the mortgage term.</td>
</tr>
<tr>
<td>A file copy of the suggested HUD Annual Adjustment Notice is sufficient to satisfy this requirement.</td>
</tr>
<tr>
<td>Should disputes arise, the HUD suggested method for evidence may not be sufficient. Lenders should instead be guided by the advice of counsel about the type and duration of record retention.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>4155.1 6.B.7.f Collection Action after ARM Adjustment</th>
</tr>
</thead>
<tbody>
<tr>
<td>The lender should notify its collections personnel of the possibility that the Annual Adjustment Notice was not received by a borrower, and of the need to take remedial action, when necessary. Collection personnel should</td>
</tr>
<tr>
<td>- make a follow up call to determine if the notice was received by the borrower, if his/her payments do not reflect the increase/decrease described in the Notice, and</td>
</tr>
<tr>
<td>- immediately mail a duplicate Notice if not received.</td>
</tr>
</tbody>
</table>
8. Failure to Provide a Timely/Accurate Annual ARM Adjustment Notice

**Introduction**

This topic contains information on the lender’s failure to provide timely or accurate Annual ARM Adjustment Notices, including

- notice failure for more than one year
- restriction on collecting payment increases
- decline of new interest rate, and
- inaccurate Annual ARM Adjustment Notice.

**Change Date**

March 24, 2011

**4155.1 6.B.8.a ARM Notice Failure for More Than One Year**

If the lender fails to provide notice to the borrower for more than one year, then it must determine an adjusted interest rate for each omitted year, because the calculations for each year affect the rate for subsequent years.

The one and two percentage point limitations and five and six percentage point caps apply to each year, and must be considered when determining the new interest rate.

Penalties will be imposed on the lender if it fails to provide borrower notification in advance of each Change Date.

**4155.1 6.B.8.b Restriction on Collecting Payment Increases on ARMs**

Although the new interest rate may increase, the lender is prevented from collecting any increase in payments until the notice has met the required 25-day advance notice requirement.

If timely notice is not provided, the

- lender forfeits its right to collect the increased amount, and
- borrower is relieved from the obligation to pay the increased payment amount.

*Continued on next page*
8. Failure to Provide a Timely/Accurate Annual ARM Adjustment Notice, Continued

4155.1 6.B.8.c  
Decline of New Interest Rate on ARMs

If the new interest rate declines, the failure of the lender to provide proper notice would result in overpayments, until the mortgage rate is properly adjusted.

In this case, the lender must refund the excess, with interest at a rate equal to the sum of the Margin and Index in effect on the Change Date, from the date of the excess payment to the date of repayment.

After the lender applies the refund to any existing delinquency, the borrower has the option of

- a cash refund, or
- applying the excess to the unpaid principal balance of the mortgage.

4155.1 6.B.8.d  
Inaccurate Annual ARM Adjustment Notice

HUD requires that errors be corrected if the

- lender miscalculates the interest rate and/or the monthly payment, and
- errors are reflected in the notice.

HUD does not take a position on whether an erroneous notice constitutes a failure to provide notice under the terms of the mortgage contract. This is a legal matter that is subject to local law and court interpretation.
9. ARM Assumptions and Transfers of Servicing

**Introduction**

This topic contains information on ARM assumptions and transfers of servicing, including

- transfers of ARMs between servicers
- disclosing ARM terms on an assumption, and
- credit review on an assumption.

**Change Date**

March 24, 2011

**4155.1 6.B.9.a Transfers of ARMs Between Servicers**

The seller is responsible for providing the transferee with complete servicing records reflecting total compliance with Adjustable Rate Mortgage (ARM) disclosure and reporting requirements.

HUD regulations require that the transferee/assignee assume all servicing obligations. However, negligent ARM lenders/transferors are not permitted to avoid disclosure obligations.

If a failure of Notice or other error is discovered, the lender/transferor holding the loan when the failure occurred is responsible for reimbursing the lender currently holding the loan, if any burden or refund to the borrower is required.

*Continued on next page*
Disclosing ARM Terms on an Assumption

Lenders should encourage sellers to disclose the terms of an existing ARM in any sales transaction. However, when an assumption takes place, both the seller and lender should assume responsibility for notifying the assumptor about the terms and conditions of the ARM.

When the lender becomes aware of an assumption, and has the name of the assumptor, it should provide the assumptor with

- a copy of the original Disclosure Statement, and
- an explanatory letter addressing the ARM obligations.

The lender should document an acknowledgement of the assumptor’s receipt of the disclosure information.

Credit Review on an Assumption

The lender must prepare a new Disclosure Statement to ensure that the assumptor is aware of the ARM obligation, when

- the assumption transaction requires a creditworthiness review, or
- a release from personal liability is requested and approved.

Processing of the following forms must be based on the interest rate in effect at the time that the complete credit review package is submitted to the Direct Endorsement (DE) Underwriter:

- Form HUD 92210, Request for Credit Approval of Substitute Mortgagor, and/or
- Form HUD 92210.1, Approval of Purchaser and Release of Seller.
10. Tracking ARMs

Introduction

This topic contains information on tracking ARMs, including

- ARM suffix codes
- DE suffix codes, and
- hybrid ARM type indicator.

Change Date

March 24, 2011

4155.1 6.B.10.a ARM Suffix Codes

In order to track Adjustable Rate Mortgage (ARM) activity, case number suffix codes (Section of the Act Automatic Data Processing (ADP) Codes) are

- indicated on all Form HUD-92900 application addendums, and
- printed on Form HUD-59100, Mortgage Insurance Certificate.

4155.1 6.B.10.b DE Suffix Codes for ARMs (Reference)

For a complete list of the Section of the Act ADP suffix codes for ARMs and other Direct Endorsement (DE) cases, see HUD 4155.2 12.B.1.a.

Continued on next page
10. Tracking ARMs, Continued

4155.1 6.B.10.c
Hybrid ARM Type Indicator

In addition to the ADP suffix codes assigned to ARMs, a hybrid ARM type indicator has been added to the FHA’s Computerized Home Underwriting Management System (CHUMS).

When submitting loan data to FHA via the FHA Connection, or its functional equivalent, the lender must identify the type of ARM, if the ARM is indicated by an ADP code, by selecting the one, three, five, seven, or ten year ARM type indicator.