
CHAPTER 5. SETTLEMENT OF CLAIMS

- 5-1. INTRODUCTION. When a claim for loss on a defaulted loan insured under Title I of the National Housing Act is received by HUD, every effort is made to process it expeditiously so that its certification for payment by the Treasury Department can be made promptly. This Chapter provides guidance to the lender in preparing its claim for submission. It not only outlines the required documents, forms, and papers, but also explains what information is necessary so that the claim can be processed, in most cases, without further correspondence. Careful adherence to these procedures will result in payment of Title I claims within a minimum of time and thereby reduce processing costs of both the lenders and HUD.
- a. Accurate and Complete Claims. If the claim submitted is accurate and complete in every detail, its examination for compliance with statutory and regulatory requirements and the verification of the allowable loss can be completed without delay. In such cases, the lender receives its check from the Treasury Department in a relatively short time. When inaccuracies and omissions require correspondence with the lender to obtain clarification or completion of information, payment of the claim is unavoidably delayed.
 - b. Data and Documentation. An accurate and complete claim requires certain data and documentation which must be obtained at the inception of the loan. Some of these requirements will vary, depending on the HUD Title I Regulations in effect at the time the application for the loan was made. It is important, therefore, that personnel engaged in initiating transactions as well as those who are responsible for preparing and submitting claims be familiar with these requirements. Chapters 1, 2 and 3 contain the administrative policies and requirements concerning the disbursement of eligible loans.
 - c. Amount Payable on Losses. The amount of claim is limited to 90 percent of the calculated principal and interest loss sustained by the lender, plus other allowances permitted by the regulations. Interest at 7 percent per annum will be computed on the outstanding principal balance from the date of default to the date of application for reimbursement of loss, or to a date nine months and 31 days from date of default, whichever period of time is the lesser. In no event shall the total interest allowances exceed the maximum permissible financing charge on the principal amount outstanding nine months and 31 days from the date of default.

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5-2. ASSEMBLING AND EXAMINING THE NECESSARY PAPERS. When the lender has exhausted all collection efforts and wishes to file claim under its contract of insurance, the first step is to assemble all documents, forms, ledger cards, and correspondence relating to the account in a file. The Transmittal Sheet of the Title I Claim for Loss in Appendix 4, page 3 provides a convenient reference in determining when the documents listed therein are required. The documents in this file should be carefully examined for completeness and the file should be carefully checked to determine that the documents listed below, as required, are included. In summary we require that the total file be submitted including your collection history and other related forms, documents and letters.

a. Credit Application, Form FH-1. This form should be examined to determine:

- (1) that it has been properly dated;
- (2) that the borrower's interest in the property improved has been clearly stated as an owner or lessee;
- (3) if lessee, that the expiration date of the lease has been indicated;
- (4) if leased commercial property, that the owner has either joined in signing the promissory note or HUD's prior credit approval was obtained (in the latter event, the approval letter should be included in the claim file);
- (5) that the description and estimated cost of the improvement(s) have been fully stated;
- (6) that the property improved, if a residential structure, had been completed and occupied for ninety days or longer;
- (7) that all other items on the form have been completed;
- (8) that the application has been properly signed by the eligibility borrower(s); and
- (9) that, if proceeds were disbursed to a dealer-contractor, the person selling the improvement(s) has signed.

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- (5-2) (10) If the examination disclosed inaccuracies or omissions, an explanation should be prepared for inclusion in the file.
- (11) The credit application submitted with the claim must be an ORIGINAL. If the original cannot be furnished or if the loan application is unsigned, a statement signed by an officer of the lending institution should be submitted, setting forth the reason(s) why a copy of the application is being included and/or from what source the information on the unsigned application was obtained for consideration of the claim.
- b. Promissory Note. The note should be examined to determine that it has been properly dated; that the payee has been stated; that the numerical and written face amounts are in agreement (if the two amounts are not in agreement, a signed statement from the makers acknowledging the true amount should be obtained); that the date of the first payment and the amount and number of periodic payments have been indicated; and that the signatures of all note signers are genuine. If the note was executed for and on behalf of a corporation, a corporate resolution should be attached empowering the makers of the note to create a binding obligation of the principal.
- c. Assignment of Note. The note on which a claim is paid is assigned in full to the United States, and 10 percent of the calculated loss will be borne by the lender. The note is not assignable even though HUD may make full recovery of the amount due on the note, nor will there be any transfer of the credit of funds in such instances. In no case may an insured lending institution ask a borrower, dealer or other person to reimburse the institution for co-insurance loss, or any other deduction made by HUD in settlement of a claim, since the National Housing Act intends that such loss will be borne by the lender. Since the lending institution is no longer holder of the note, it has no legal basis for requesting the obligor to make further payment. Any amounts received on account by the lending institution after claim must be forwarded promptly to HUD.
- (1) The reverse of the note should be examined to assure that it bears a complete endorsement of the dealer-contractor (if it is a dealer loan) and that the assignment to the United States of America by the lender indicates the name of the lending institution, is signed by an authorized official with title indicated, and is dated.

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- (5-2) (2) The reverse of the note shall be in the following form:

"All right, title and interest of the undersigned is hereby assigned (without warranty, except that the note qualifies for insurance) to the United States of America.

(Lending Institution)

By:

Title:

Date:

- d. Borrower's and Dealer's Completion Certificate, Form FH-2. The complete certificate should be examined to determine that it has been completely executed and signed by an eligible borrower and by the person approved by the lender as the dealer. As in the case of the promissory note, signatures to the certificate must be genuine. This certificate is not to be signed or dated until after the improvements have been satisfactorily completed by the dealer. This document is not required for direct loans.
- e. Dealer's Contract or Sales Agreement. The contract or sales agreement should be inspected to determine that a complete description of the material to be used and the work to be performed has been stated; that the unit cost is shown; and that the stated cost of the improvement(s) is in agreement with the credit application. The contract or sales agreement must be signed by an eligible borrower and by the dealer, although the signatures appearing on the original. The date of the contract or sales agreement should be prior to the commencement of the improvements and should bear a close relationship to other required dealer documentation. This document is not required for direct loans.
- f. Advance Notice to Borrower. At least six (6) calendar days prior to making disbursement to a dealer, the lender must give the borrower written notice of the approval of his/her credit application. This document is not required for direct loans.
- (1) If additional improvements are made, a supplemental advance notice must be sent to the borrower. In any

event, it is not required that the borrower acknowledge receipt of such notice(s).

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- (5-2) (2) The lender must, however, produce a record of having mailed or delivered such notice(s). As acceptable records of delivery would be a dated carbon copy of the notice(s) or a dated entry in the borrower's loan file.
- (3) Supplies of the advance notice are not furnished by HUD. Lenders should issue the notice on their own letterhead stationery.
- g. Borrower's Authorization Certificate. Where proceeds are paid to someone other than the borrower, the authorization certificate should be inspected to determine that it has been completely executed and signed by all borrowers and all makers and co-signers on the note. As in the case of the promissory note, the signatures of all parties to the certificate must be genuine. This document is not required for direct loans.
- h. Demand Letter. A final demand letter must be sent to the borrower(s) and a copy made a part of the claim file. The demand letter should be unconditional and for the full unpaid balance of the note. To avoid forms of demand letters which are not wholly acceptable, the following phrasing is suggested:
- "The option to accelerate maturity of your note is exercised at this time, by reason of the fact that periodic payments have not been made in accordance with its terms. The entire balance of \$_____ plus interest of \$_____, making a total of \$_____ is now due and payable."
- i. Ledger Cards. If the borrower had prior Title I loans with outstanding balances at the time the defaulted note was made, the file should contain a ledger card on the earlier obligations. If claim is being filed on a defaulted note which had been refinanced, the ledger card covering the prior loan refinanced, clearly stating the unpaid balance and the amount of rebate, should be made a part of the claim file.
- (1) Certified Statements in Lieu of Ledger Cards. If the lender has converted to automatic data processing, certified statements executed by an official of the

institution are acceptable alternatives to payment records itemized on ledger cards.

- (5-2) (2) Statement Certification. As applicable, and for compliance with specific regulations, the statements should certify as follows:
- (a) That a prior loan was not past due more than 15 days when proceeds of a later loan were disbursed;
 - (b) That the outstanding aggregate loan balance with respect to the same property or structure did not exceed the dollar limitation prescribed for the type of loan involved;
 - (c) That the total outstanding principal balance on all Title I loans at one time did not exceed the dollar limitation set for the type of loan having the largest permissible limit, exclusive of financing charges. If in excess of the largest permissible limit, a letter granting prior approval of the Assistant Secretary for Housing-Federal Housing Commissioner should be in the file.
- j. Attorney's Papers. When an attorney was employed to effect collection and the claim is to include attorney's fees actually incurred and paid, a complete statement from the attorney should be obtained and made a part of the file. A transcript of the judgment should also be included in the file when the note was reduced to a judgment. For further information on judgments and attorney's papers, see paragraph 4-4 of this Handbook.
- k. Proof of Claim. The lender is required to service loans in accordance with acceptable practices of prudent lending institutions. This, of course, includes timely filing of Proof of Claim in decedent estate and bankruptcy cases. If a Proof of Claim in a decedent estate or bankruptcy action is filed with the administrator or referee, a copy of such Proof of Claim should also be in the claim file.
- (1) Bankruptcy. The assignment of the Proof of Claim in bankruptcy should identify the District Court by District and Division; cite the names of all bankrupts; show the bankruptcy number, the United States of America as assignee, the amount of the claim, the

corporate name of the lender; and bear the signature and title of an authorized official (i.e. an officer of the lending institution).

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(5-2) (2) Decedent Estate. The assignment of the Proof of Claim in a decedent's estate should identify the administrator or executor; show the name of the deceased, the United States of America as assignee, the amount of claim, and the corporate name of the lender; and bear the signature and title of an authorized official.

l. Certificate of Eligibility, FH-1(HP). Loans made available under the Historical Preservation category shall be made only for the rehabilitation, preservation or restoration of historic structures. The proposed improvement(s) to the historic structure shall be submitted to the State Historic Preservation Officer of any other person authorized by the Secretary of the Interior in the state where the historic structure is located. If the proposal, is approved, the approval should be indicated on the FH-1(HP) and made a part of the claim file upon submission to HUD for insurance benefits. (Reference Section 201.1606 of the Title I Regulations.)

m. Evidence of Fire Safety Marshal's Approval. Loans insured under the Fire Safety Equipment category shall be considered only where a proposal has been submitted and approved by the Fire Safety Marshal or other State or local official or agency, or other authority having primary responsibility or jurisdiction for the fire safety requirements of the health care facility. This document shall be made a part of the claim file when claim is submitted on a defaulted Fire Safety Equipment Loan. (Reference Section 201.1125(a) of the Title I Regulations.)

n. Additional Documents. While the aforementioned documents represent the basic papers required for loans insured under Title I, additional forms and certificates are necessary under certain circumstances. These and the applicable Title I Regulations are:

(1) Letter granting prior approval of the Assistant Secretary for Housing-Federal Housing Commissioner, Sections 201.5(e) and 201.1611;

(2) Certificate of Eligibility, Form FH-801, on loans which

include built-in-kitchen appliances, Section 201.6(d)(6);

- (3) Statement of Eligibility, Form FHA-226, on loans which include civil defense shelters, Section 201.6(e);

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- (4) Certification of loans which include septic tanks, Section 201.6(f);

- (5) Certificate of Eligibility, Form FH-802, on loans which include permanently installed carpeting, Section 201.6(g).

5-3. SECURITY INSTRUMENTS. If security has been taken in the form of a real estate mortgage, deed of trust, conditional sales contract, chattel mortgage, mechanics lien, or other security device for the purpose of securing the loan, it should be recorded in accordance with the statutes of the applicable jurisdiction. Where security has been recorded the insured shall, prior to filing claim, place on record an assignment to the United States of America of said security. A \$25 fee will be paid the lender for expenses in recording any security or other recordable assignment to the United States of America. In those instances where the lender or its attorney is of the opinion that the assignment should not be recorded, the lender should include in its submission of claim a full explanation of the reason the assignment was not recorded, and if circumstances warrant, the Regulations will be waived. A waiver, however, cannot be considered unless a complete statement of the operative facts is included with the claim submission.

- a. Assignment of Security. While a marginal form of assignment, similar to that used in assigning a note, is acceptable in some jurisdictions, it has been found that in most instances a separate form of assignment which fully identifies the security is required. The local recording office can advise lenders of the requirements in the applicable jurisdiction.
- b. Preparation. Unavoidable delays will be eliminated if the assignment is prepared as indicated below. The assignment should:
 - (1) Cite a nominal consideration;
 - (2) Designate the United States of America as assignee;

- (3) Follow the instrument for description of the property;
- (4) Show recording references, i.e., date, book, page;
- (5) Show the name of the lender, be dated, and signed by an authorized official;

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- (6) Bear the corporate seal;
- (7) Be acknowledged and dated by a Notary Public.

5-4. JUDGMENTS. While the regulations do not specifically require a lender to litigate on a Title I note, there are instances wherein a judgment is required to establish the validity and enforceability of the obligation. In addition, from a collection standpoint, and from facts singular to a particular transaction, the lender should consider the advisability of instituting legal action.

a. Assignment of Judgment. The assignment of the judgment should be prepared from a copy of the transcript and should provide the data indicated below. As in the case of other security, the Clerk of the Court for the local jurisdiction can advise lenders regarding the requirements for an acceptable assignment to transfer interest. The assignment should:

- (1) Cite a nominal consideration;
- (2) Designate the United States of America as assignee;
- (3) Identify the court by name, state and county;
- (4) Fully cite the awards of the court, i.e., principle, interest, fees and costs;
- (5) Recite the true balance due on the total judgment in the covenant;
- (6) Show the name of the lender, be dated, and signed by an authorized official;
- (7) Bear the corporate seal;
- (8) Be acknowledged and dated by a Notary Public.

b. Attorney's Statement of Collections. In all instances,

where an attorney is engaged, the full amount collected by the attorney should be credited to the account, and the file should contain a statement from the attorney itemizing the amounts and dates of payments collected and the cost of such collections. Attorney's fees for collections are reimbursable only if paid by the lender. unique to the Fire Safety Equipment Loans, attorney's fees shall not exceed \$250. The attorney's fees for the remaining Title I

improvement loans are limited to 25% of the amount collected by the attorney on the defaulted note (excluding recording expenses), provided the borrower is liable for the payment of such fees under the laws of the jurisdiction applicable to the note, and provided the lender does not waive its claim against the borrower for such fees.

- (1) All payments received after the maturity of the note, including the amount collected by the attorney, should be itemized in the space provided on the Title I Claim for Loss, Schedule A-Deductions, Section III, (See appendix 4, page 7).
 - (2) The full amount collected by the attorney and attorney's fees should be shown on the Title I Claim for Loss, Schedule B-Additions, Section III (See appendix 4, page 9).
- c. Attorney's Statement of Fees. In all instances, the fees incurred must be supported by a receipted bill from the attorney.
- (1) In accordance with Property Improvement Loan, attorney's fees for a judgment secured by confession after default are limited to \$10 or 15% of the balance due on the note, whichever is the lesser.
 - (2) Attorney's fees for a judgment secured through suit are limited to \$50 or 15% of the balance due on the note, whichever is lesser. This does not apply to Fire Safety Equipment Loans.
 - (3) Attorney's fee for collections and expenses incurred by an attorney for Fire Safety Equipment Loan litigations shall not exceed \$250 per case.
- d. Attorney's Waiver of Lien. Examine to determine that the Attorney's Lien included in the judgment has been satisfied

or waived; if waived, that the statement waives all rights of subsequent claim, and that the statement has been signed by the attorney.

- 5-5. TITLE I CLAIM FOR LOSS (HUD-637). When the examination of the claim papers has been completed, the next step is the preparation of the HUD-637, which is designed to accommodate all Title I loans. This package includes a cover sheet and four sets of forms as follows: Transmittal Sheet (Parts 1 and 2), Application Voucher (Parts 3 thru 6), Schedule A-Deductions (Parts 7 thru 10) and Schedule B-Additions (parts 11 thru 14).

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Schedules A and B shall be completed prior to entering date on the Application Voucher. The schedules consist of three sections; however, all Title I property improvement loans covered in this Handbook are to use Section III on both schedules, leaving Sections I and II blank.

- a. Mandatory Completions. The Transmittal Sheet and both Schedules A and B (applicable section only) must be completed. Lenders who do not wish to complete the "total insured loss" under block 16 on the Application Voucher must, at a minimum, complete blocks 1 thru 15 and 17 thru 19. Only items 1, 3, and 5 are mandatory items under block 16.
- b. Time Requirements. Claim shall be filed no later than 6 months after the due date of the final installment provided for in the note where a Property Improvement Loan or Historical Preservation Loan has defaulted. Where a Fire Safety Equipment Loan has defaulted, claim shall be filed no later than 9 months and 31 days after the due date of the earliest fully unpaid installment provided for in the obligation. Unless an extension of the claim filing period is requested by the lender and approved by the Secretary, the above claim filing periods must be met according to regulatory requirements. Request for such extensions must be in writing and submitted to the Director, Office of Title I Insured Loans. Attach an approved copy of the extension request to the claim package.
- c. Payments received after Filing Claim. Should the maker of the obligation tender payments thereon to the insured institution subsequent to the filing of this application, such monies will be accepted for, and proceeds immediately transmitted to Director, Mortgage Insurance Accounting, OFA, Attention: Receipts and Deposits Branch, Department of Housing and Urban Development, Washington, DC 20410, in

accordance with the HUD Regulations.

- 5-6. COMPUTATION OF INSURED LOSS. Information required by the forms in the claim package is sufficient for the lender to compute the total insured loss. After having completed the Transmittal Letter, Section III of Schedules A and B, and the upper portion of the Application Voucher (blocks 1 thru 15), the lender may enter its computation in the column headed "Certified Information furnished by Applicant" (block 16). It is not mandatory that the lender compute the total insured loss under block 16 of the application voucher (See paragraph 4-5a). If the lender elects to compute the total insured loss (block 16), a verification of the lender's computations is made upon receipt of the claim package by HUD. Where discrepancies are detected

during the verification process, HUD will enter corrections in the column headed "HUD USE ONLY" , Verification of Amount Due. Parts 4, 7, and 12 are returned to the lender, indicating any alterations made to the claim, with the Treasury check issued in payment of the claim.

- 5-7. EXAMPLE OF COMPUTATION OF INSURED LOSS WHERE UNEARNED FINANCE CHARGE IS COMPUTED BY THE " RULE OF 78'S METHOD". The following hypothetical case is prepared for the information of lenders to illustrate the manner in which loss is determined on defaulted Title I property improvement loans. Let us assume that a 10 year Historical Preservation note for \$51,660, payable in 120 monthly installments of \$430.50 with date of first payment August 1, 1977 was executed July 1, 1977. The financing charge (at 12% per annum) of \$21,660 was taken using the factor tables in paragraph 2-16. The borrower received \$30,000 (net proceeds) in cash. Installments were paid when due up to and including the payment of April 1, 1979, but the May payment was not made. On June 30, 1979, the lender, having received no further payments, demanded full payment of the balance of the note. On July 31, 1979, the lender decided to submit a claim and furnish the information and documentation required by the Title I Claim for Loss, Form HUD-637. The case discussed here, is illustrated in Appendix 4, pages 3, 5, 7, and 9.

- a. Schedule A- Deductions, Section III. Since no additional funds were received after the date of default, no amounts will be entered in this section. Normally, the total amount of principal and interest received by the lender on account of the loan from any source, which has not been applied in reduction of the borrower's indebtedness, would be entered here. NOTE: The refund of insurance premiums listed as

item 1 does not include Title I insurance charge. The Title I insurance charge adjustments, if any, will be computed by HUD and applied on a future Title I Billing Statement, Form FHA-761.

- b. Schedule B-Additions, Section III. Since this claim involved a secured loan, no litigation actions were entered. This section is used to itemize each allowable expenditure incurred by the lender while processing the defaulted loan. A statement of expenses and receipts shall be included for each time entered in this section of the claim form.
- c. Application Voucher. Based on the information contained in the claim file, complete blocks 1 thru 15. The computation for items listed under block 16 is made in accordance with the following comments and is inserted on the Application Voucher as illustrated on page 5 of Appendix 4. The item

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(5-7) numbers listed below relate to the numbers in the left margin of the Application Voucher.

Item No.	Comments
(1)	Enter the total finance charge which has been included in the face amount of the note. Example: Face amount of Note (\$51,660) less proceeds to borrower (\$30,000) equals total finance charge (\$21,660).
(2)	The finance charge is considered distributed over the period of the loan and is prorated to the date of default. The proration is based on the outstanding balance for the total period of time from the date of the note. Twenty-one of the one hundred twenty regular payments were received, the default being in the twenty-second period. The factor to be used, therefore, is .3321861233 based on the formula is subparagraph 4-7d. The charge to be prorated (\$21,660) multiplied by this factor represents the finance charge earned to default. The amount that will be allowed under this claim is \$7,195.15 (\$21,660 x .3321861233).
(3 & 4)	The loan proceeds paid to the borrower of \$30,000 added to the earned finance charge of \$7,195.15 yielded \$37,195.15.
(5 & 6A)	Since \$9,040.50 was received in regular

installments, this amount is subtracted from the total amount due up to the time of default, leaving a balance due of \$28,154.65.

- (6B) This line is to be used when the regulations require that the finance charge be calculated by the "actuarial method" and an amortization schedule is used.
- (7 & 8) No additional deductions were listed on Schedule A, therefore, enter a zero on line 7 and bring down the amount shown on line 6A.
- (9) Interest at 7% was due, therefore, on \$28,154.65 from May 1, 1979 to July 31, 1979, the date on which the claim was filed. The table headed "Exact Number of Days in Fractional Parts of a Year" (see Appendix 4, page 15) shows the total number of days between May 1, 1979 and July 31,

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- (5-7) 1979 to be 91. The interest factor for 91 days at 7% per annum as shown in the interest table (see Appendix 4, page 16) is .0174521. This factor, when multiplied by the outstanding balance due as of May 1, 1979, (\$28,154.65) results in interest for this period of \$491.36.
- (10) Add lines 8 and 9 to arrive at the unpaid principal balance (including the prorated finance charge) and the uncollected earned interest.
- (11 & 12) No allowable expenses were listed in section III of Schedule B. Enter a zero here, then bring the figure from line 10 down to line 12.
- (13 & 14) Since the Historic Preservation Loan is considered a "type A" loan, enter 10% of line 10, Unpaid Principal Balance and Earned Interest, on line 13. Subtract the computed 10% (\$2,864.60) from line 12 (\$28,646.01) for the Total Insured Loss (\$25,781.41) on line 14.

Blocks 17, 18, and 19 shall contain the full name and address (including ZIP code) of the lending institution, signature and title of the authorized official attesting to the certification statement, and the date the application is signed, respectively.

- d. "Rules of 78's" Formula for Determining Earned Finance Charge Proration Factor. Outlined below is the formula for determining the proration factor required to compute the earned finance charge to the date of default.

- (1) m = number of days to first payment
n = number of periods in loan
d = number of payments made before default

$$\frac{mn + dn - d(1 + d)}{30 \times 2} = \text{Proration Factor}$$

$$\frac{mn + n(n-1)}{30 \times 2}$$

- (2) To illustrate how this formula is used, the following shows how the factor was determined for the hypothetical case explained in subparagraph c (Item 2) above and illustrated in Appendix 4, page 5.

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$$\frac{31 \times 120 + 21 \times 120 - 21(1 + 21)}{30 \times 2} = .3321861233$$

$$\frac{31 \times 120 + 120(120 - 1)}{30 \times 2}$$

- 5-8. THE "ACTUARIAL" METHOD. Section 201.1265 of the HUD Regulations mandates the method of calculation that must be used to determine the earned and the corresponding unearned interest (finance charge on a defaulted Fire Safety Equipment Loan. According to this section of the Regulations, the insured lender shall be calculated according to the "actuarial" method. This method of interest computation treats each loan exactly as though it were an interest bearing, direct reduction loan. Thus, with the use of a standard direct reduction loan amortization schedule or a table of actuarial refund factors, the amount or earned/unearned interest can be determined.

- a. The amortization schedule is a useful guide for both the borrower and the lender. The schedule provides the whole picture for a loan: (1) the monthly payment; (2) how much each payment during the entire life of the loan is divided between interest and principal; and (3) how much of the loan is outstanding at any time.

- (1) The amount of earned interest can be determined by simply accumulating the interest listed in the interest column of the schedule up to, but not including, the date of default. The following example shows the amount of interest earned on a \$1,000 loan financed at 11% for 20 years which defaulted on the 15th installment. The example is based on the amortization schedule in Appendix 4, page 10.

\$109.28 = Interest for 12 months as totaled on the schedule.
9.03 = Interest for 13th installment.
9.02 = Interest for 14th installment.
8.71 = Partial interest earned in 15th installment.
(\$9.01/.30 days = .30 x 29 days = \$8.71)
\$136.04 = Interest Earned Up to Date of Default

- (2) The instructions immediately preceding block 16 of the Application Voucher (See Appendix 4, page 12) states, in part "Where the 'Actuarial Method' is used, start with line 6B..." This instruction applies only when the amortization schedule is used to determine the earned/unearned interest. The amount to be placed on line 6B is the unpaid principal balance shown on the schedule as of the last fully paid installment, plus

any interest earned in the following (default) period. Using the example from (1) above the amortization schedule in Appendix 4, page 10, the unpaid principal balance to be placed on line item 6B of the Application Voucher is determined as follows:

\$982.71 = Balance as of the last fully paid installment.
8.71 = Interest earned up to date of default (29 days).
\$991.42 = Unpaid Principal Balance as of Date of Default.

- b. Actuarial refund tables provide another convenient source of exactness in this process of interest computation. Once the number of unpaid installments are determined, the appropriate factor can be located on the refund table and applied against the monthly installment figure. The answer (amount of unearned interest) should then be subtracted from the total amount of interest to obtain the amount of earned interest up to the date of default. Detailed instructions for the use of the tables are explained below. Paragraph 5-9c, item (2) shows an illustration.

- (1) Compute the number of full payments remaining to maturity. This would be the number of payments still remaining less one (do not count the payment on the date of default). Because interest is considered earned up to the date of default, the number of days between the last fully paid installment and the date of default (but not including the date of default) are earned interest days. Thus, the date of default should be added on the payments remaining as one day.
- (2) From the Amortization Refund Tables, find the page for the appropriate annual percentage rate. Under the heading "months", find the number of full payments remaining. Add to this factor, the daily factor which represents the day of default. Multiply the resulting factor times the monthly installment. This is the amount of unearned interest (finance charge).
- (3) Subtract the amount of unearned interest from the total amount of interest calculated for the full term loan to obtain the amount of earned interest.

5-9. EXAMPLE OF COMPUTATION OF INSURED LOSS WHERE UNEARNED FINANCE CHARGE IS COMPUTED BY THE "ACTUARIAL METHOD" USING ACTUARIAL REFUND TABLES. Let us assume that a 20 year, \$50,000 (net

(5-9) proceeds to be entered in block 11 of the Application Voucher) Fire Safety Equipment Loan financed at 11% per annum interest rate, payable in 240 monthly installments of \$516.10 with date of first payment August 20, 1977 was executed July 20, 1977. Installments were paid when due up to and including the payment of September 30, 1978, but the October payment was not made. On November 30, 1978, the lender, having received no further payments, demanded full payment of the balance of the note. On December 28, 1978, the lender decided to submit a claim and furnished the information and documentation required by the Title I Claim for Loss, Form HUD-637. The case discussed here is illustrated in Appendix 4, pages 11 through 14.

- a. Schedule A- Deductions, Section III. No additional funds were received after the date of default; therefore, no entry will be made in Schedule A. (See paragraph 4-7a.)
- b. Schedule B- Additions, Section III. No expenses were incurred as a result of processing this claim. (See paragraph 5-7b).

- c. Application Voucher. Blocks 1 through 15 of the case illustrated in Appendix 4, page 12, were based on information contained in the claim file. Completion of all items under block 16 by the lender are optional. It is required, however, that the lender, at a minimum, complete items 1, 3, and 5 of block 16.

- (1) Although the instructions preceding block 16 recommends starting the calculations on line 6B when the actuarial method is used, all items (1 through 14) under block 16 have been completed in this example to add clarity and is recommended to lenders who elect to completely calculate the total insured loss with the use of the actuarial refund tables.
- (2) The computation for items listed under block 16 were made in accordance with the following comments and inserted on the voucher. The item numbers listed below relate to the numbers in the left margin of the voucher.

Item (1) - In this case, the total finance charge is obtained by multiplying the monthly installment figure times the number of installments required to amortize the loan (see block 12) less the amount of proceeds to the borrower.

Monthly Installment \$ 516.10

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(5-9)	Installments Required	x	240
			<hr/>
			\$123,864.00
	Proceeds to Borrower	-	50,000.00
			<hr/>
	Total Finance Charge		\$ 73,864.00

Item (2) - The earned finance charge is obtained by first determining the unearned finance charge which is then subtracted from the total finance charge shown in item 1, above.

- (a) Compute the number of full payments remaining to maturity:

Original Number of Installments	
Required to Amortize Loan	240
Number of Installments Made	-14
	<hr/>
Number of Installments Remaining	226
Installment Due on Date of Default	- 1
	<hr/>

- (b) For interest purposes, one (1) day will be added to the number of full installments remaining, which represents the day of default on which interest is not earned by the lender.
- (c) With the use of the appropriate actuarial refund table (see Appendix 4, pages 17 and 18), locate the factor for the 225th month. Add to this factor one (1) daily factor. Then multiply the sum of the factors times the monthly installment for the unearned interest.

Monthly Factor	Daily Factor		
129.909371	+ 0.028696	=	129.93806
		x	516.10
			Monthly Installment
			<hr/>
			\$67,061.03
			Unearned Finance Charge

- (d) Subtract from the total finance charge (item 1) the unearned finance charge to determine the earned finance charge of "Charge Prorated to Default", (item 2).

Total Finance Charge	\$73,864.00
Unearned Finance Charge	-67,061.03
	<hr/>
Charge Prorated to Default	\$ 6,802.97

Items (3 and 4) - The total proceeds to the borrower should be entered in block 11 and as item 3 under block 16. Add items 2 and 3 to determine the amount of principal and

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- (5-9) earned finance charge due the insured up to the time of default.

Items (5 and 6B) - The number of monthly installments received on this loan prior to maturity totaled 14. This number is placed in the line provided by item 5. A total of \$7,225.40 (\$516.10 x 14) was received in regular installments. This amount is subtracted from the amount due up to the time of default, leaving a balance due of \$49,577.57.

Items (7 and 8) - Enter zero on line 7. Bring the amount shown on line 6 down to line 8.

Item (9) - Interest at 7% was due on the outstanding balance, computed from the date of default to the date of the claim application. For the purpose of determining the date of default, the Regulations provide: "any payment

received on an account, including payments on judgements predicated thereon, shall be applied to the earliest unpaid installment."

(a) The table headed "Exact Number of Days in Fractional Parts of a Year" (see Appendix 4, page 15) shows the total number of days between October 20, 1978 and December 28, 1978 to be 69. The interest factor for 69 days at 7% per annum as shown in the interest table (see Appendix 4, page 16) is .0132329. This factor, when multiplied by the outstanding balance as of the date of default, results in the earned interest for this period.

(b) $\$49,577.57 \times .013239 = \656.06 (enter as item 9).

Item (10) - Add items 8 and 9. The answer (\$50,233.63) is entered as item 10.

Item (11 and 12) - Enter zero on line 11. Bring the amount shown on line 10 down to line 12.

Item (13) - Since the Fire Safety Equipment Loan is considered a "Type A" loan, enter 10% of item 10 as item 13 (\$5,023.36).

Item (14) - Subtract item 13 from item 12 for the total insured loss and enter the answer on line 14 (\$45,210.27).

Blocks 17, 18, and 19 shall contain the full name and address (including ZIP code) of the lending institution,

signature and title of the authorized official attesting to the certification statement, and the date the application is signed, respectively

5-10. CANCELLATION OF VOLUNTARY REPURCHASE OF CLAIMS. A claim may be withdrawn upon return of the Treasury check. In the event the check has been accepted for deposit, the insured may voluntarily repurchase the claim by submitting its official check for the claim amount, provided in each instance the transaction is consummated not later than 31 days from the date the Treasury check was received by the lender.

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