

Transfers of Mortgages--Participations[FOIA Exemption 6: Names of Private Parties Withheld]

Legal Opinion: GHM-0094

Subject: Transfers of Mortgages--Participations  
[FOIA Exemption 6: Names of Private Parties Withheld]

December 8, 1993

, Esq.

Street, N.W.  
Washington, DC

Dear Mr. :

This responds to your recent series of letters, commencing September 14, 1993, regarding paragraph 1-33 of Handbook 4435.01 REV-1, Project Construction and Servicing Before Final Closing. Paragraph 1-33 deals with the assignment of insured mortgages and your letters question the validity of certain provisions in subparagraph's (B) and (D) thereof. You have contended that the Handbook contravenes the HUD regulation at 24 C.F.R. Section 207.261 because: (1) it requires HUD approval in advance of mortgage transfers where they occur after full disbursement; and (2) it precludes the transfer of a partial interest in an insured mortgage or pool of insured mortgages under a participation agreement or arrangement, which transfer results in 100% participation by others, unless HUD approval is obtained. As set forth in more detail below, we agree that these Handbook provisions are not correct as currently written.

Paragraph 1-33(B) presently states, among other things, that the Department's Field Office Manager must give written approval before a mortgagee may transfer an insured mortgage after full disbursement. This, however, is not consistent with the Department's current regulations, nor with other Handbook guidance.

The basic provision governing the assignment of insured mortgages is 24 C.F.R. Section 207.261. Subsection (a) thereof provides that an approved mortgagee may assign, transfer or pledge an insured mortgage or a partial interest in an insured mortgage in accordance with the terms and conditions of that regulation. Transfers of insured mortgages prior to, and after, full disbursement are treated differently by 24 C.F.R. Section 207.261. In this regard, 24 C.F.R. Section 207.261(c) provides that transfers or pledges of insured loans prior to full disbursement may be made "only with the prior written approval of the Commissioner." In comparison, 24 C.F.R. Section 207.261(d), which deals with transfers after full disbursement, does not mention prior HUD approval. Rather, it states that:

Transfers after full disbursement may be made only to a transferee approved by the Commissioner. Upon assumption by

the transferee of all obligations under the contract of

mortgage insurance, the transferor shall be released from its obligations under such contract. The transfer shall be reported to the Commissioner on a form satisfactory to the Commissioner.

Thus, 24 C.F.R. Section 207.261(d) establishes two basic requirements for transfers of insured mortgages after full disbursement, namely, that: (1) the transfer be made only to an FHA-approved mortgagee; and (2) the transfer be reported to the Department. Paragraph 2-27(a) of Handbook 4350.4, Insured Multifamily Mortgage Servicing and Field Office Remote Monitoring Handbook, affirms this implementation by providing that whenever there is a sale of a HUD-insured mortgage, HUD should be advised on Form HUD-92080 within 15 calendar days of the action. Thus, based on the language of 24 C.F.R. Section 207.261(d) as well as on its implementation in paragraph 2-27(a) of Handbook 4350.4, after full disbursement a mortgagee need not receive HUD's written approval before it may transfer an insured mortgage. To the extent that paragraph 1-33 of Handbook 4435.01 REV-1 conflicts with this position, it should not be followed.

The second issue concerns paragraph 1-33(D) of Handbook 4435.01 REV-1. Paragraph 1-33(D) presently states that a mortgagee may transfer a partial interest in an insured mortgage or pool of insured mortgages under a participation agreement or arrangement, without obtaining HUD approval, subject to, among other things, total participation by others not exceeding 90% before final closing and 95% after final closing. Paragraph 1-33(D) also provides that, under certain conditions, the Field Office Manager may approve 100% participation by others before or after final closing.

We agree that these requirements, as presently set forth in paragraph 1-33(D), also are incorrect. As you are aware, 24 C.F.R. Section 207.261 used to require that, where a mortgagee of record wished to transfer a partial interest in an insured mortgage without HUD approval, the mortgagee had to retain at least a 10% beneficial interest in the insured mortgage up to the time of final endorsement, and at least a 5% beneficial interest thereafter. On August 11, 1986, however, the Department amended 24 C.F.R. Section 207.261 to, among other things, eliminate these percentage limitations on participation by others in an insured mortgage. See 51 Fed. Reg. 28699 (Aug. 11, 1986). Accordingly, 24 C.F.R. Section 207.261(e), which deals with transfers of partial interests under participation agreements, presently reads as follows:

A partial interest in an insured mortgage or pool of insured mortgages may be transferred under a participation agreement or arrangement (such as a declaration of trust or the issuance of pass-through certificates), without obtaining

the approval of the Commissioner, if the following conditions are met:

(1) Legal title to the insured mortgage or mortgages shall be held by an approved mortgagee which, for the purposes of this paragraph (e), shall be referred to as the principal mortgagee;

(2) The participation agreement, declaration of trust or other instrument under which the partial interest is transferred shall provide that:

(i) The principal mortgagee shall remain mortgagee of record under the contract of mortgage insurance;

(ii) The Commissioner shall have no obligation to recognize or deal with anyone other than the principal mortgagee with respect to the rights, benefits, and obligations of the mortgagee under the contract of mortgage insurance; and

(iii) The mortgagor shall have no obligation to recognize or do business with anyone other than the principal mortgagee or its servicing agent with respect to rights, benefits, and obligations of the mortgagor or the mortgagee under the mortgage.

Paragraph 1-33(D) of the Handbook appears to have been drafted with the regulation, i.e., section 207.261(e), as it existed prior to August 11, 1986, in mind. In this regard, paragraph 1-33(D) does not reflect consideration of that August 11, 1986 regulation change which, among other things, removed the percentage limitations on participation by others from section 207.261(e). Further, in correspondence issued after such 1986 amendment of section 207.261(e), the Department has interpreted that section as permitting an FHA-approved mortgagee to transfer, without prior HUD approval, up to 100% of the beneficial interest in a HUD insured mortgage provided that the conditions set forth in subsections 207.261(e)(1) and (2) are satisfied and that legal title to the insured mortgage, at the time of the participation, remains with the principal mortgagee of record.

As presently written, paragraph 1-33(D) conflicts with this interpretation of the regulation because it does not permit (without HUD approval) 100% participation interests where the conditions of subsections 207.261(e)(1) and (2) are met. Thus, paragraph 1-33(D) should not be followed to the extent that it: (1) mandates that a mortgagee may transfer a partial interest in an insured mortgage or pool of insured mortgages under a

participation agreement or arrangement, without obtaining HUD approval, only if the total participation by others does not exceed 90% before final closing and 95% thereafter; and (2) requires HUD approval for 100% participation by others before or after final closing where the conditions of subsections 207.261(e)(1) and (2) are satisfied and legal title

to the insured mortgage, at the time of the participation,  
remains with the principal mortgagee of record.

We have consulted with the Office of Housing on this matter. The Office of Housing has advised us that paragraph 1-33 will be revised to follow the positions set forth in this letter. In the interim, for any closings that may arise before the revisions to paragraph 1-33 are finalized and issued, this letter will serve to indicate the Department's position that paragraph's 1-33(B) and 1-33(D) of Handbook 4435.01 REV-1 are in error and that the legal positions set forth in this letter should be followed.

Very sincerely yours,

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