FHA's Office of Single Family Housing

Temporary Procedures FHA Connection Data Entry—HECM with Negative Residual Income

Last Updated: August 25, 2015

Temporary Procedures for HECMs with Negative Residual Income and FAQs on Residual Income and Compensating Factors

In establishing the HECM Financial Assessment system requirements for FHA Connection (FHAC), FHA provided functionality for mortgagees to enter the type of compensating factors considered in the underwriting decision. The system requirements did not, however, allow Mortgagees to enter a negative number in the “Residual Income” data field section, or to enter income available from compensating factors that would supplement the mortgagor’s residual income.

Temporary procedures will be available as of August 31, 2015, to allow the entry of a negative residual income amount in the FHA Connection “Residual Income” field for HECMs that require a Financial Assessment.

HECMs Closed Prior to FHAC Ability to Accept HECM with Negative Residual Income

For HECMs closed prior to August 31, 2015with negative residual income, that could not be delivered prior to making the system change, mortgagees may request a refund of MIP Late Charges and Interest when performing Loan Set Up in the HERMIT system.

To request a refund of MIP Late Charges and Interest, logon to the HERMIT system and complete the following steps:

Step 1. Select the Loan tab.
Step 2. Enter the FHA case number of the loan. Click Search.
Step 3. Click Setup link beside the loan displayed under the Loan Search Results section.
Step 4. The Loan Setup screen is displayed.
Step 5. Enter a closing date under the Loan Dates section (this date must be 15 days prior to the current date for the late charge occurrence or 30 days prior to current date for occurrence of penalty interest) for the Late Charge and Penalty Interest section to be displayed at the bottom of the screen.
Step 6. Select the Refund Request checkbox.
Step 7. In the Refund Comments box, enter “FHAC HECM Financial Assessment Update screen was unable to accept a negative residual income amount.”
Step 8. Complete Loan Setup of the case, by entering all other required details. Click Save & Next.
Step 9. The refund request is added on the loan and displayed on the Refunds screen under Accounting tab with a status of Pending.
Step 10. The HUD SF Premiums Manager can now select the loan and approve or deny the refund.

FAQs on Residual Income and Compensating Factors

All loans requiring use of these temporary procedures must meet all requirements set forth in Mortgagee Letter 2014-21 and Mortgagee Letter 2014-22 and attached Financial Assessment and Property Charge Guide.

Must a mortgagee document the existence of all listed criteria for use of compensating factors?

The criteria for selecting any or all compensating factors included in the HECM Financial Assessment and Property Charge Guide has not changed. Compensating Factors may be checked in FHA Connection only where all of the criteria specified for the Compensating Factor in Section 4.2 of the HECM Financial Assessment and Property Charge Guide have been met.

How must income from other sources be documented?

Any income from other sources that is added to the mortgagor's income must meet the documentation standards described in the HECM Financial Assessment and Property Charge Guide. Income that does not meet these documentation standards may not be considered.

What are the requirements for documenting Property Charge Payment History as a compensating factor?

The mortgagee must determine that the mortgagor meets all of the following:

- mortgagor residual income is 80%-99% of the applicable amount for his or her family size and geographic region on the Table of Residual Income in Section 3.100;
- mortgagor has paid his or her own property charges directly for at least the last 24 months (i.e., they were not paid by a mortgagee from an escrow account) and meets the standard in Section 2.28;
- all property charge payments have been made without incurring penalties during the last 24 months; and
- current income is not less than income during the previous 24 months.

If a mortgagor meets the requirements specified in the second, third and fourth bullets above, but the mortgagor's residual income does not equal or exceed 80% of the applicable amount for his or her family size and geographic region on the Table of Residual Income in Section 3.100, mortgagees may not select this compensating factor. All four requirements must be met.

May a mortgagee use any compensating factors that are not defined in the Guide?

No, the compensating factors described in Section 4.2 of the HECM Financial Assessment and Property Charge Guide are the only compensating factors that may be cited.

What factors should be considered when determining if the mortgagor meets the Residual Income Standard?

The Residual Income standards and compensating factors that can be used in determining whether the mortgagor meets the applicable residual income standards for their region and family size are published in the HECM Financial Assessment and Property Charge Guide. In Mortgagee Letter 2014-21, FHA stated that mortgagees “must perform a cash flow/residual income analysis, in accordance with FHA guidelines, to determine the capacity of the mortgagor to meet his, or her, documented financial obligations and comply with the mortgage provisions.”

Does the Residual Income calculation in FHAC include reduction in property charge expenses or additional income from Life Expectancy Set Aside (LESA) Funds?

No, the calculation in FHAC is based on the mortgagor’s income and expense analysis, including compensating factors.

What are the requirements for documenting factors that were considered in making the Financial Assessment and Property Charge Set Aside decisions.

As stated in Section 4.3 of the HECM Financial Assessment and Property Charge Guide, mortgagees must document any extenuating circumstances to address derogatory credit and property charge payment history, and or compensating factors to support residual income shortfalls.

Mortgagees must identify in writing on the Financial Assessment Worksheet all specific circumstances and factors it relied upon to make its favorable determination, including the effect of a required LESA. Supporting documentation must be included in the origination binder.