

*Announcement 04-03*

*June 24, 2004*

*Amends these Guides: Selling and Servicing*

*Uniform Residential Loan Application, Servicing Agreements, Commitment Pair-Offs, Prepayment Premiums, Flexible 97® Mortgages, Flexible 100™ Mortgages, Manufactured Housing Update, Test Period for Revised Appraisal Report Forms, and Possible Lapse of National Flood Insurance Authority*

This Announcement discusses Selling and Servicing Guide changes that update, clarify, or amend our current requirements or update policies that have been impacted by recent federal regulations. The topics are:

- clarification of a Federal Reserve Board requirement impacting residential loan applications;
- clarification of our requirements when a lender plans to sell a loan to Fannie Mae and another lender is the current servicer;
- changes to the lender-requested commitment pair-off process;
- clarification of our prepayment premium provisions;
- updated information regarding down payments for Flexible 97 and Flexible 100 mortgages;
- updated information on titling manufactured housing as real property;
- details concerning three test appraisal report forms; and
- selling and servicing loans should the National Flood Insurance Program Authority lapse.

## ***Uniform Residential Loan Application, Form 1003***

On March 18, 2003, in the official staff commentary to Regulation B, Section 202(7)(d)(1)-3, the Federal Reserve Board set forth certain guidance to lenders on how to evidence applicants' intent to apply for joint credit. The Federal Reserve Board staff commentary has been clarified to provide that a person's intent to be a joint applicant for credit must be evidenced at the time of application and should be documented in some fashion. Although signatures on "borrower" and "co-borrower" lines of the Fannie Mae/Freddie Mac residential loan application (form 1003/65) generally evidence intent to apply jointly for credit, a creditor could always obtain additional evidence of intent, such as a specific written indication from the applicants.

Fannie Mae is *not* revising the *Uniform Residential Loan Application*, Form 1003, to provide space for additional information to evidence intent to apply for joint credit. However, we will allow lenders to amend the form by including space for this information on page 4 of Form 1003. We consider this an authorized change that would not result in the form being treated as a nonstandard document. Other approaches, such as including this information on a separate document, are also acceptable to Fannie Mae, provided they meet the requirements of applicable law. Lenders should consult counsel to determine their alternatives.

## **Servicing Agreements**

Each lender's Mortgage Selling and Servicing Contract provides that servicing is a contractual relationship between the lender and Fannie Mae (as owner of all right, title, and interest in mortgages the lender has delivered to us) that is established for particular mortgages when we acquire them. The following reinforces our policy that there may not be any servicing agreement with any other party that pre-exists delivery of loans to Fannie Mae and that conflicts with the foregoing Mortgage Selling and Servicing Contract principle. Of course, a lender may assign servicing from itself to another Fannie Mae-approved servicer concurrent with delivery of mortgages to Fannie Mae, or the lender may utilize a subservicer that is a Fannie Mae-approved servicer if the lender is our servicer after such delivery, in either case pursuant to the lender's Mortgage Selling and Servicing Contract and as specifically provided in our Guides. Further, such assignee servicer or subservicer may be the party that serviced the loans before delivery of them to Fannie Mae.

Selling Guide Part I: Lender Relationships; Chapter 2, Contractual Relationship; Section 203, Assignment of Servicing. The following text replaces Section 203:

When we purchase or securitize whole mortgages or participation pool mortgages, we allow a lender that does not want to service the mortgages to assign automatically the servicing of the mortgages to another Fannie Mae-approved lender that is approved to service the particular type of mortgages for which the servicing is being assigned. The lender notifies us of the assignment of servicing by designating the 9-digit lender identification number that Fannie Mae has assigned to the assignee servicer on the *Loan Schedule* (Form 1068 or 1069) or the *Schedule of Mortgages* (Form

2005) and, if required, by including in its delivery package mortgage assignments prepared in accordance with Part IV, Section 402, of this Guide. If the servicer that will service the mortgages for Fannie Mae is servicing the mortgages for the lender before the lender delivers the mortgages to Fannie Mae, and the contractual relationship between the lender and the servicer is such that no assignment is legally necessary, then the lender may simply designate the servicer by notifying us as above described.

An assignment of servicing should be documented by a separate contract between the lender and the assignee servicer that provides (among other things) for the transfer of the servicing of the mortgages as of an effective date that is not later than the date we purchase the mortgages for our portfolio or the issue date for the MBS pool. (If the transfer of actual servicing responsibilities from the lender to the assignee servicer has not already taken place, but will become effective concurrent with our purchase or securitization of the mortgages, we expect the transfer to take place in accordance with the requirements for transfers of servicing that are included in Part I, Section 205, of the Servicing Guide.)

By designating another lender as servicer of the mortgages on the *Loan Schedule* (Form 1068 or 1069) or the *Schedule of Mortgages* (Form 2005), the lender represents and warrants that with respect to such mortgages: (a) the servicer has agreed to service the mortgages for Fannie Mae, and (b) the provisions of any agreement between the lender and any other party providing for servicing the mortgages will not continue after the date on which Fannie Mae funds the cash delivery or issues the MBS.

By accepting an assignment of servicing of the mortgages or a designation as servicer, the servicer: (a) agrees to service the mortgages in accordance with all Fannie Mae requirements, (b) represents and warrants that the provisions of any agreement between the servicer and any other party providing for servicing the mortgages will not continue after the date on which Fannie Mae funds the cash delivery or issues the MBS, and (c) assumes responsibility for all of the lender's contractual obligations related to the mortgages, including all selling warranties and any other liabilities that arise in connection with the origination of the mortgages or the servicing of the mortgages prior to the delivery of the mortgages to Fannie Mae. The lender is not released, however, from any liabilities to Fannie Mae with respect to the mortgages or the servicing of them prior to the delivery of the mortgages to Fannie Mae. Both the lender and the servicer will be jointly and severally liable to Fannie Mae for the obligations and liabilities related to the mortgages that arise before delivery of the mortgages to Fannie Mae.

We also allow a lender that is servicing the mortgages it delivers to us to use acceptable computer service bureaus or tax services to perform some of the servicing functions. We will hold the servicer fully accountable, however, for any actions taken (or not taken when required) by these companies.

After we have purchased or securitized a mortgage (or a participation interest in one), we must approve all subsequent assignments of servicing related to that

mortgage (or participation interest) before the servicing can be transferred.

Selling Guide Part I: Lender Relationships; Chapter 2, Contractual Relationship; Section 204, Use of Subservicers; and Servicing Guide Part I: Lender Relationships; Chapter 2, Contractual Relationship; Section 206, Use of Subservicers. The following two bullets are added to these Guide sections to become the second and third bullets in those sections:

- The master servicer represents and warrants that with respect to the mortgages subserviced by the subservicer: (a) the subservicer will service the mortgages in accordance with all Fannie Mae requirements, and (b) the provisions of any agreement between the lender and any other party providing for servicing the mortgages will not continue after the date on which Fannie Mae funds the cash delivery or issues the MBS except as a subservicing agreement that does not conflict with Fannie Mae's servicing requirements.
- By agreeing to subservice mortgages owned by Fannie Mae, the subservicer: (a) agrees to service the mortgages in accordance with all Fannie Mae requirements, and (b) represents and warrants that the provisions of any agreement between the lender and any other party providing for servicing the mortgages will not continue after the date on which Fannie Mae funds the cash delivery or issues the MBS except as a subservicing agreement that does not conflict with Fannie Mae's servicing requirements.

Selling Guide Part II: Delivery Options; Chapter 1, Cash Deliveries. The following text replaces the current Selling Guide text for the second paragraph of the Chapter that appears just before Section 101:

By submitting a whole mortgage or a participation pool mortgage to us as a cash delivery, the lender represents, warrants, and agrees that all right, title, and interest in the mortgage is sold, transferred, set over, and otherwise conveyed by the lender to Fannie Mae as of the date of our funding of the purchase proceeds. The lender further represents and warrants that there is no agreement with any other party providing for servicing the mortgage that will continue after such date unless there is full compliance with all our Guide requirements that provide for subservicing (see Selling Guide Part I, Chapter 2, Section 204 and Servicing Guide Part I, Chapter 2, Section 206). The party that was servicing for the lender prior to such date may become our servicer, however, if there is full compliance with all our Guide requirements that provide for assignment of servicing from the lender concurrent with conveyance of the mortgage to us (see Selling Guide Part I, Chapter 2, Section 203). Both the lender and Fannie Mae intend for all cash deliveries to Fannie Mae to be absolute sales.

Selling Guide Part II: Delivery Options; Chapter 2, MBS Pool Deliveries. The following text replaces the current Selling Guide text for the paragraph that appears just before Section 201 and starts with "Both the lender and Fannie Mae intend...":

Both the lender and Fannie Mae intend for all MBS pool deliveries to Fannie Mae to

be absolute sales. By submitting a whole mortgage (or a participation interest in a mortgage) to us as an MBS pool delivery, the lender represents, warrants, and agrees that all right, title, and interest in the mortgage (or participation interest) is sold, transferred, set over, and otherwise conveyed by the lender to Fannie Mae as of the issue date of the MBS. The lender further represents and warrants that there is no agreement with any other party providing for servicing the mortgage (or participation interest) that will continue after such date unless there is full compliance with all our Guide requirements that provide for subservicing (Selling Guide Part 1, Chapter 2, Section 204 and Servicing Guide Part I, Chapter 2, Section 206). The party that was servicing for the lender prior to such date may become our servicer, however, if there is full compliance with all our Guide requirements that provide for assignment of servicing from the lender concurrent with conveyance of the mortgage to us (see Selling Guide Part I, Chapter 2, Section 203). The lender also warrants that the mortgage (or participation interest) conforms to the requirements and specifications we have in place for mortgages that are pooled to back MBS issues, that the mortgage satisfies the general mortgage eligibility requirements and underwriting guidelines for mortgages delivered to Fannie Mae, that the description of the mortgage (or participation interest) set out in the applicable delivery documents is true and correct, and that all owners named in the delivery instructions were provided the most recent Prospectus (and any applicable Prospectus Supplement) that was available at the time they entered into their contract for the purchase of the related securities.

## **Lender-Requested Commitment Pair-Offs**

Selling Guide Part III: Mortgage Commitments; Chapter 3, Portfolio Cash Commitments; Section 309.03, Lender-Requested Commitment Pair-offs. Chapter 3 provides information about the commitments that are available for cash deliveries of whole mortgages or participation pool mortgages, including the procedures for obtaining them. Since the most recent Selling Guide Update (June 30, 2002), the name of Fannie Mae's Cash Commitment Window has changed to the Whole Loan Desk, and the process for obtaining a commitment also has changed. As a result, we are revising the Guide text to explain the process a lender must now use to purchase (pair off) all or part of a mandatory delivery commitment if it is unable to deliver enough mortgages to satisfy our minimum delivery requirement. The following text replaces Section 309.03 of the Selling Guide in its entirety.

A lender may purchase (pair off) all or part of a mandatory delivery commitment if it is unable to deliver enough mortgages to satisfy our minimum delivery requirement. The pair-off request can be made at any time between the date the commitment is first executed and the date on which the contract will expire.

A lender may request a full or partial pair-off of a mandatory delivery commitment through eCommitting or by calling the Whole Loan Desk at 1-800-752-1080. eCommitting and the Whole Loan Desk are available between 9:00 a.m. and 5:00 p.m. (Eastern time) on any business day. All telephone conversations will be voice recorded.

When pairing out of a contract using eCommitting, the following information will be needed:

- a user id, password, and PIN # for eCommitting;
- a commitment number for the contract to be paired off;
- an indication of whether the request is for a full or partial pair-off; and
- the aggregate unpaid principal balance of the mortgages that the lender would like to pair off.

Once a pair-off quote is requested by clicking on the “Calculate Fee” button within the commitment pair-off section of eCommitting, the lender must accept the fee quotation within a short interval (currently 60 seconds) if it wants to exercise the pair-off. (The lender may obtain a confirmation of the pair-off in the “View Commitment Fees” section of eCommitting). If the lender does not accept the fee quotation within the short interval, our pair-off offer becomes null and void. The lender may obtain a new quotation within eCommitting at a later time – before the contract expiration date – to avoid an automatic extension and the possible assessment of an automatic pair-off fee.

When pairing out of a contract while calling the Whole Loan Desk, the following information will be needed:

- the caller’s name and telephone number;
- the lender’s name and nine-digit Fannie Mae Seller number under which the commitment was taken;
- a commitment number for the contract to be paired off;
- an indication of whether the request is for a full or partial pair-off; and
- the aggregate unpaid principal balance of the mortgages that the lender would like to pair off.

We will verify the information provided, calculate the applicable pair-off fee, and give the lender our pair-off fee quotation. The lender must accept the fee quotation within a short interval if it wants to exercise the pair-off. (The lender may obtain a confirmation of the pair-off in the “View Commitment Fees” section of eCommitting.) If the lender does not accept the fee quotation within the short interval, our pair-off offer becomes null and void. The lender may obtain a new quotation by calling us at a later time — before the contract expiration date — to avoid an automatic extension and the possible assessment of an automatic pair-off fee.

Our calculation of the pair-off fee will take the following into consideration:

- the remaining commitment period;
- the market movement of prices and/or yields at the time of commitment versus the time of pair-off; and
- the amount to be paired off.

To take advantage of these pair-off procedures, a lender needs to have electronic drafting procedures in place for the payment of commitment fees. The lender should prepare the *Authorization for Automatic Transfer of Funds* (Form 1072) to establish electronic drafting arrangements if it does not already have such arrangements established. (See Exhibit 2 of this Chapter 3 for procedures on establishing drafting arrangements.)

## Requirements for Mortgage Loan Documents

A significant part of our effort to create sustainable homeownership opportunities is the re-examination of Fannie Mae's standards for loans we purchase or securitize. The policies outlined below relating to prepayment premiums derive from our commitment, among other things, to ensure that the terms and conditions of mortgages and other agreements are fair and balanced for all parties in the transaction.

### Prepayment Premiums

Selling Guide Part IV: Mortgage Documents; Chapter 2, Mortgage or Deed of Trust Notes; Section 201.02, Prepayment Provision. Our Selling Guide states that a borrower who wants a lower monthly payment or lower closing costs might agree to accept a mortgage loan that includes a prepayment premium in connection with an early pay off of the mortgage loan. In the past, we purchased loans with a prepayment premium provision so long as all of the following applied:

- The mortgage loan was delivered under a negotiated contract.
- The mortgage loan provided some benefit to the borrower for accepting the prepayment premium.
- The borrower was offered the choice of another mortgage loan product that did not require a prepayment premium.
- The terms of the prepayment provision were adequately disclosed to the borrower.
- The prepayment premium would not be charged when the mortgage debt was accelerated as the result of the borrower's default in making his or her mortgage loan payments.

In the interest of providing added assurance that Fannie Mae purchases or securitizes only those prepayment premium loans that confer a benefit to the borrower and in determining whether a requested commitment is acceptable, a loan sold to Fannie Mae shall not carry a prepayment premium term that exceeds three years. Lenders are encouraged to agree to waive all or part of the prepayment premium if a prepayment premium is required because the home is sold. At the time of Fannie Mae purchase or securitization, lenders are required to elect whether to waive all or part of the prepayment premium in the event that the home is sold and shall notify the borrower of such an election to waive the premium. Lenders are reminded that prepayment premiums are not permissible on our Expanded Approval<sup>TM</sup>/Timely Payment Rewards<sup>®</sup> mortgages.

These policies will apply to all loans delivered to Fannie Mae on or after September 1, 2004.

## **Flexible 97 Mortgages and Flexible 100 Mortgages**

Selling Guide Part VII: Mortgage Eligibility; Chapter 1, Conventional Mortgages; Section 113, Flexible 97 Mortgages and Flexible 100 Mortgages. With the release of Desktop Underwriter® Version 5.3.1, we introduced an enhancement to the Flexible 100 mortgage by modifying the minimum contribution requirements to allow borrowers to contribute as little as \$500 of their own funds to the transaction. With the release of Desktop Underwriter Version 5.4, we announced that mortgages with LTVs up to 100 percent that have interested party contributions up to 3 percent are now eligible for MBS delivery. We are updating Section 113.01, Down Payment, to reflect these changes.

A borrower who obtains a Flexible 100 mortgage does not have to make a down payment; however, he or she must make a minimum contribution toward the payment of closing costs and prepaid items. The borrower has the option of either making a minimum contribution of at least 3 percent of the property's sales price from approved Flexible sources or making a minimum contribution of \$500 from his or her own funds. Approved Flexible sources for this 3 percent contribution may come from the borrower's personal savings; a secured loan backed by a certificate of deposit, 401(k) account, the cash value of a life insurance policy, or other real estate; a Community Seconds® subsidized second mortgage; a gift or unsecured loan from a relative, domestic partner, fiancé, or fiancée; or a gift, grant, or unsecured loan from an employer, a church, a public agency, or a nonprofit organization (other than a credit union). The borrower's minimum contribution may not come from an interested party contribution, premium pricing, or any other type of unsecured debt. Interested party contributions (or premium pricing) up to 3 percent of the property's sales price are permitted to be used to cover closing costs above the borrower's minimum contribution. Mortgages with LTVs up to 100 percent that have interested party contributions up to 3 percent are eligible for MBS delivery.

## **Manufactured Housing Update**

In Announcement 03-06, Fannie Mae stated its intention to provide lenders with information on titling manufactured housing as real property in all 50 states. To date, information on 39 states has been posted on our web site. The remainder should be available by the end of the summer. The web site provides guidance to lenders on obtaining real property liens on new or previously owned manufactured homes (and the land on which they are situated) that secure purchase money or refinance loans. It also offers information on obtaining a certificate of title to the manufactured home, if one is required, and on surrendering the certificate of title, where that is possible. To access this information on the current web site, go to [www.efanniemae.com](http://www.efanniemae.com), scroll down to Single-Family and click on Originating and Underwriting, then in the center column, under Reference Tools and Information, click on Manufactured Housing Titling. This will bring up the chart that allows users to reach information on specific states. Lenders should be aware that future changes in the web site could affect the specific procedures for access to this information.



## Test Period for Revised Appraisal Report Forms

In Announcement 04-02 dated June 1, 2004, we released three test appraisal report forms for a comment period as part of a three-stage process. We are releasing today the following test appraisal report forms as the second stage of that process:

- ***Exterior-Only Inspection Residential Appraisal Report*** (Fannie Mae Test Form 2055 dated June 2004);
- ***Individual Cooperative Interest Appraisal Report*** (Fannie Mae Test Form 1073 dated June 2004); and
- ***Exterior-Only Inspection Individual Cooperative Interest Appraisal Report*** (Fannie Mae Test Form 1075 dated June 2004).

These test forms will enable the appraiser to report the results of his or her appraisal in a more concise manner than our existing report formats. Direct questions have been added to the report forms, which require the appraiser to comment on key areas of his or her research and analysis. The revised forms require the appraiser to report in a clear and succinct yes/no format whether the property has any apparent physical deficiencies or conditions and to determine if such conditions affect the livability, soundness, or structural integrity of the property. The sale history section of the report form also has been expanded to accommodate space for a three-year history for the subject property and the comparable sales as well as space for reporting the appraiser's analysis of the listing and sale history.

The revised format allows the appraiser to report his or her conclusions in a brief but comprehensive manner, which will be more efficient for reviewing and processing. All of our standard applicable exhibits that are used to support an appraisal based on the particular property inspection type also are required when using these test forms. We made a variety of enhancements to these test forms to help communicate our expectations for a high-quality appraisal, to strengthen the appraiser's accountability for the quality of his or her appraisal, and to help ensure the appraiser's compliance with our requirements and those of the Uniform Standards of Professional Appraisal Practice.

A copy of each of these test forms is enclosed. Any lender or appraiser who wants to participate in the testing of these report forms and/or provide comments may do so. Comments can be submitted to us (either by sending them in an E-mail message addressed to [test\\_appraisal\\_forms@fanniemae.com](mailto:test_appraisal_forms@fanniemae.com) or by regular mail addressed to Fannie Mae, Test Appraisal Forms, 3900 Wisconsin Avenue, NW, Mail Stop 2H-4S-08, Washington, DC 20016) no later than **October 1, 2004**. *Lenders and appraisers may continue to use the test appraisal report forms until June 1, 2005 for purposes of satisfying Fannie Mae's appraisal requirements.*

Our goal is to consolidate the number of our appraisal report forms in order to simplify our documentation requirements for customers and their appraisers. Accordingly, when we release the final approved report forms after the test period, we will be retiring certain existing appraisal report forms and using the form numbers currently associated with those forms for different appraisal report and inspection purposes. We will have one appraisal report form for reporting an appraisal for each of the following purposes. As a result,

lenders and appraisers will be able to determine which test appraisal report forms should be used based upon the type of property and property inspection required.

- ***Uniform Residential Appraisal Report*** (Fannie Mae Test Form 1004 dated May 2004) for one-unit appraisals based on an interior and exterior property inspection;
- ***Definitions, Statement of Limiting Conditions, and Appraiser's Certification*** (Fannie Mae Test Form 1004B dated May 2004) for use with all one- to four-unit appraisal reports;
- ***Exterior-Only Inspection Residential Appraisal Report*** (Fannie Mae Test Form 2055 dated June 2004) for one-unit appraisals based on an exterior-only property inspection;
- ***Manufactured Home Appraisal Report*** (Fannie Mae Test Form 1004C to be released by August 2004) for one-unit manufactured home appraisals based on an interior and exterior property inspection;
- ***Individual Cooperative Interest Appraisal Report*** (Fannie Mae Test Form 1073 dated June 2004) for an appraisal of an individual cooperative unit based on an interior and exterior property inspection;
- ***Exterior-Only Inspection Individual Cooperative Interest Appraisal Report*** (Fannie Mae Test Form 1075 dated June 2004) for an appraisal of an individual cooperative unit based on an exterior-only property inspection;
- ***Appraisal Update and/or Completion Report*** (Fannie Mae Test Form 1004D dated May 2004) for use with all one- to four-unit appraisal reports;
- ***Small Residential Income Property Appraisal Report*** (Fannie Mae Test Form 1025 to be released by August 2004) for appraisals of two- to four-unit properties based on an interior and exterior property inspection; and
- ***Two- to Four-Unit Residential Appraisal Field Review Report*** (Fannie Mae Test Form 2000A to be released by August 2004) for appraisal field reviews for two- to four-unit appraisal reports.

## **Possible Lapse of National Flood Insurance Program Authority**

In December 2002, when it appeared that flood insurance under the National Flood Insurance Program (NFIP) would not be available after January 1, 2003 due to the fact that Congress did not provide funding prior to adjournment, Fannie Mae issued Announcement 02-14, instructing lenders on procedures to follow during the hiatus. While legislation renewing the NFIP has been passed by Congress and is awaiting Presidential signature, should NFIP authority lapse, the directions we gave lenders in Announcement 02-14 will again become applicable.

If NFIP funding is not renewed, lenders should:

- work with borrowers to ensure, to the extent possible, that applications for flood insurance and premium payments are received by FEMA prior to the date of lapse; and
- take all possible steps to facilitate issuance of coverage as soon as possible once the NFIP insurance authority is renewed, including submitting applications and tendering premiums.

Lenders should refer to Announcement 02-14 for more specific guidance.

Fannie Mae will continue, on a temporary basis, to purchase loans secured by properties located in Special Flood Hazard Areas that do not have flood insurance. This policy will apply to loans originated during the hiatus period and delivered to us until the earlier to occur of July 15, 2004 or the reauthorization of the NFIP. While Fannie Mae is willing to purchase loans under these conditions, lenders are advised to consult counsel to determine that they have requisite authority to originate or otherwise deal in such loans. Further, we strongly suggest that borrowers be advised prior to closing of their risk if a flood damages their property during the period of non-insurance.

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The changes described in this Announcement are immediately effective unless otherwise indicated. In addition, unless otherwise directed, lenders should discuss questions about the topics in this Announcement with their Customer Account Managers.

Pamela S. Johnson  
Senior Vice President

Enclosures