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24 CFR Part 202

Revisions to FHA Credit Watch Termination Initiative; Proposed Rule

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 202

[Docket No. FR–4625–P–01]

RIN 2502–AH60

Revisions to FHA Credit Watch Termination Initiative

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Proposed rule.

SUMMARY: This proposed rule would make several amendments to the Federal Housing Administration (FHA) Credit Watch Termination Initiative. The proposed rule provides for a fully computerized Credit Watch status notification process through use of the FHA Neighborhood Watch Early Warning System. A mortgagee will be considered to be on Credit Watch status if, at any time, it has a default and claim rate of higher than 150 percent of the normal rate, and its origination approval agreement has not been terminated. The proposed rule would also prohibit a mortgagee that has received a notice of proposed termination of its origination approval agreement from establishing a new branch for the origination of FHA-insured mortgages in the lending area covered by the proposed termination. In addition, the proposed rule would establish that the default and claim thresholds underlying the Credit Watch Termination Initiative apply to both underwriting and originating mortgagees. The proposed rule would also codify the definition of ''underserved area'' that is currently used under the Credit Watch Termination Initiative. Finally, the proposed rule would provide that, for purposes of Credit Watch Termination evaluation, the date of mortgage origination will be considered to be the date the loan transaction commences amortization, rather than the date of endorsement for FHA mortgage insurance.

DATES: *Comment Due Date:* June 2, 2003.

ADDRESSES: Interested persons are invited to submit comments regarding this proposed rule to the Regulations Division, Room 10276, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410–0500. Comments should refer to the above docket number and title. A copy of each comment submitted will be available for public inspection and copying between 7:30 a.m. and 5:30 p.m. weekdays at the above address. Facsimile (FAX) comments are not acceptable.

FOR FURTHER INFORMATION CONTACT: Phillip Murray, Director, Office of Lender Activities and Program Compliance, Office of Housing, Department of Housing and Urban Development, 451 Seventh Street, SW., Room B–133, Washington, DC 20410; telephone (202) 708–1515 (this is not a toll-free number). Persons with hearing or speech impairments may access this number via TTY by calling the toll-free Federal Information Relay Service at 1–800–877–8339.

SUPPLEMENTARY INFORMATION:

I. Background—The FHA Credit Watch Termination Initiative

Homeownership rates in the United States have reached a record level, and the efficient management of the FHA mortgage insurance fund remains a cornerstone of HUD's strategy to further expand housing opportunities. By originating and underwriting insured single family mortgages in accordance with program guidelines, FHA-approved mortgagees are valuable participants in achieving greater access to the housing credit market, particularly for individuals and in geographic areas that have traditionally been under-served.

Approval of a mortgagee by HUD/FHA to participate in FHA mortgage insurance programs includes an origination approval agreement (the Agreement) between HUD and the mortgagee. Under the Agreement, the mortgagee is authorized to originate single family mortgage loans and submit them to FHA for insurance endorsement. Some mortgagees, however, have demonstrated high default and claim rates on their FHA-insured portfolios that, although not signifying violations of FHA requirements, are nonetheless unacceptable. As a result, HUD developed the Credit Watch Termination Initiative to identify mortgagees with unsatisfactory performance levels and take ameliorative action at an early stage. HUD's regulations for the Credit Watch Termination Initiative are found at 24 CFR 202.3.

Under the FHA Credit Watch Termination Initiative, FHA systematically reviews mortgagees' early default and claim rates, that is, defaults and claims on mortgagees' loans during the initial 24 months following endorsement. Mortgagees with excessive default and claim rates are considered to be on Credit Watch Status and, in cases of more severe performance deficiencies, HUD may terminate the mortgagee's loan origination approval authority. Credit Watch Status constitutes a warning to a mortgagee that its default and claim rates are in excess of permissible levels, and that failure to achieve improvement may lead to the termination of its Agreement. The Termination of a mortgagee's Agreement is separate and apart from any action taken by HUD's Mortgagee Review Board for violations of FHA requirements under 24 CFR part 25.

In a May 17, 1999, **Federal Register** notice (64 FR 26769) HUD advised that it would publish a list of mortgagees that have had their Agreements terminated. HUD has periodically published such notices since May 1999.

II. This Proposed Rule

This proposed rule would make several amendments to HUD's regulations for the FHA Credit Watch Termination Initiative. The proposed changes would strengthen HUD's capacity to safeguard the FHA mortgage insurance fund. This section of the preamble describes the most significant amendments that would be made by the proposed rule.

A. Electronic Notification of Credit Watch Status

Consistent with the goals of the Administration regarding the increased use of technology in government, the proposed rule would allow for electronic Credit Watch monitoring and notification. Specifically, the proposed rule provides that HUD will, on an ongoing basis, review the FHA mortgage claim and default rate of each mortgagee in the geographic region served by a HUD field office. HUD will use its electronic Neighborhood Watch Early Warning System for this purpose. The Neighborhood Watch Early Warning System is available to mortgagees via the FHA Connection at *https://entp.hud.gov/clas/index.html*. This proposed regulatory change would codify the policy first announced in FHA Mortgagee Letter 2001–23, issued on October 21, 2001.[1] This Mortgagee Letter provides instructions for using the Neighborhood Watch Early Warning System for purposes of monitoring performance under the Credit Watch Termination Initiative. A copy of HUD

[1] The availability of the Neighborhood Watch Early Warning System was first announced in Mortgagee Letter 2000–20, issued on June 6, 2000. Mortagagee Letter 2002–15, issued on July 17, 2002, announces the list of enhancements that have been made to the Neighborhood Watch Early Warning System since issuance of Mortgagee Letter 2000–20. Copies of both these Mortgagee Letters may be obtained via the Internet at *http://www.hudclips.org*.

Mortgagee Letter 2001–23 may be obtained through HUD's Client Information and Policy Systems (HUDCLIPS) Internet Home page at *http://www.hudclips.org*.

HUD will no longer provide mortgagees with written notification of placement on Credit Watch Status. Rather, each mortgagee will be responsible for using the Neighborhood Watch Early Warning System to monitor its performance. A mortgagee will be considered to be on Credit Watch Status if, at any time, it has a rate of defaults and claims on insured mortgages originated, underwritten or both in the geographic area served by a HUD field office which exceeds 150 percent of the normal rate, and its Agreement has not been terminated by HUD. Further, the Neighborhood Watch Early Warning System, which is updated monthly, will allow the ongoing tracking of mortgagee performance, allowing for the elimination of the current six-month tracking period for evaluating mortgagees placed on Credit Watch Status.

B. Default and Claim Rates for Placement on Credit Watch Status

Under the current regulation, a mortgagee may be placed on Credit Watch Status if it has a rate of defaults and claims on insured mortgages which exceeds ''150 percent but not 200 percent of the normal rate.'' The regulation, therefore, establishes a ''cap'' on the default and claim rates for placing a mortgagee on Credit Watch Status. The existing regulation also authorizes HUD to terminate a mortgagee's Agreement if the mortgagee's default and claim rate exceeds 200 percent of the normal rate.

In the past, HUD has used its administrative discretion to focus its resources on those mortgagees with default and claim rates higher than the 200 percent threshold. This has had the potential to create a gap in HUD's Credit Watch monitoring and enforcement efforts, since mortgagees with default and claim rates falling between 200 percent of the normal rate and the higher threshold being used for terminations would neither be placed on Credit Watch Status nor have their Agreements terminated. HUD addressed this potential concern by issuing a series of regulatory waivers of the Credit Watch cap to authorize placement of such mortgagees on Credit Watch Status. This proposed rule would eliminate the need for these regulatory waivers by removing the cap, and providing that a mortgagee will be considered to be on Credit Watch Status if, at any time, it has a rate of defaults and claims on insured mortgages that exceeds 150 percent of the normal rate and its Agreement has not been terminated.

The proposed change would not restrict HUD's ability to terminate a mortgagee whose claim and default rate exceeds 200 percent of the normal rate, but merely provides that such mortgagees will be considered to be on Credit Watch Status unless HUD determines that termination may be appropriate.

C. Limitation on the Establishment of New Branches

In reviewing the Credit Watch Termination process, HUD learned that some mortgagees were establishing new branches for the origination of FHA-insured mortgages subsequent to receiving proposed termination notices for existing branches. The mortgagees would establish the new branches to replace the authority which was lost, or which might be lost, as a result of the proposed termination of the existing branches. The result was that these mortgagees were able to evade the intended effects of the Credit Watch Termination Initiative. HUD's interest is in the mortgagee determining the reasons for its high default and claim rate in a lending area and correcting the underlying causes that led to the termination before the mortgagee is allowed to establish a new branch for the origination of FHA-insured mortgages.

In order for FHA to effectively address this evasion of the intended effect of Credit Watch Termination, this proposed rule would prohibit a mortgagee that receives a notice of proposed termination of its Agreement from establishing a new branch for the origination of FHA-insured mortgages in the lending area covered by the proposed termination notice. Upon the effective date of this regulation at the final rule stage, a mortgagee that is in receipt of a notice of proposed termination may not establish any new branch in the location(s) cited in the proposed termination notice until either: (1) The proposed termination notice is rescinded; or (2) the Agreement for the affected branch or branches has been terminated for at least six months and the Secretary has determined that the underlying causes for termination have been remedied.

D. Inclusion of Underwriting Mortgagees

Under the current Credit Watch Termination regulation, HUD evaluates the performance of a mortgagee based solely on the loans it originates. HUD's Credit Watch Termination evaluation, therefore, excludes underwriting which is an important part of the mortgage loan process. While the mortgagee that originates a loan may also be the mortgagee that underwrites the loan, often there are two different entities involved. Specifically, an FHA approved loan correspondent only originates loans and does not underwrite. Rather, the loan correspondent has ''sponsor mortgagees'' that perform the underwriting function.

HUD's emphasis on accountability extends beyond the origination of loans to include the mortgagee that underwrites the loan. For example, HUD's regulations provide for the termination of a mortgagee's ability to underwrite FHA loans when the Agreement is terminated pursuant to the Credit Watch Termination Initiative (*see* 24 CFR 203.3(d)(2)(iv)). HUD has determined that to minimize the risk associated with the FHA single family mortgage insurance programs, HUD should also periodically evaluate the performance of underwriting mortgagees. Accordingly, this proposed rule would include underwriting mortgagees within the scope of the Credit Watch Termination Initiative. The proposed amendment would emphasize HUD's authority to terminate the ability of a mortgagee to originate or underwrite FHA-insured single family mortgages where the mortgagee has demonstrated an unacceptably high default and claim rate. HUD will analyze data for mortgagees that underwrite their own loans, and for mortgagees that underwrite loans for their loan correspondents as well as for mortgagees that underwrite both their own loans and loans for their loan correspondents.

E. Mortgage Origination Date

Under the current regulations for the Credit Watch Termination Initiative, a mortgage is considered to be originated in the same federal fiscal year in which HUD endorses it for FHA mortgage insurance. Although HUD requires that the mortgagee submit a mortgage for endorsement within 60 days after closing (*see* § 203.255(b)), there may be delays in the submission of the endorsement packages. Consequently, the endorsement dates for loans originated during the same period can vary greatly. Given these discrepancies in the timing of endorsement, linking the date of origination to the endorsement date does not allow for the most accurate comparison of loan performance.

This proposed rule would provide that, for purposes of the Credit Watch

Termination evaluation, the date of mortgage origination will be considered to be the date the loan transaction commences amortization, rather than the date of endorsement for FHA mortgage insurance. Unlike the date of endorsement, the beginning amortization date is not dependent on the filing of timely paperwork with HUD. Further, Credit Watch analysis is based on default and claim rates. The due date for mortgage payments is established pursuant to the closing date, and mortgage defaults are reported based on these payment due dates. Accordingly, HUD believes that focusing on the amortization date will provide for a more uniform starting date for Credit Watch evaluations and increase the effectiveness of the Credit Watch Termination Initiative.

F. Definition of Underserved Area

HUD's regulation provides that before notification of proposed termination is sent to a mortgagee, the Secretary will review the Census tract area concentrations of the default and claims. This provision of the existing regulations would not be modified by this proposed rule. If the Secretary determines that the excessive rate is the result of mortgage lending in underserved areas, the Secretary may determine not to terminate the origination approval agreement. HUD is aware, however, that predatory lending abuses may occur in underserved areas, and that the excessive rates may be the result of predatory lending. The Secretary will consider this factor, where appropriate, in making a determination.

HUD has announced in Mortgagee Letter 99–15 that, for purposes of the Credit Watch Termination Initiative, the term ''underserved area'' will have the same meaning as that provided in HUD's regulations for the Government Sponsored Enterprises at 24 CFR part 81. Specifically, § 81.2 of those regulations defines the term ''underserved area'', in part, to mean:

> [A] Census tract, a federal or state American Indian reservation or tribal or individual trust land, or the balance of a census tract excluding the area within any federal or state American Indian reservation or tribal or individual trust land, having:
>
> (i) A median income at or below 120 percent of the median income of the metropolitan area and a minority population of 30 percent or greater; or
>
> (ii) A median income at or below 90 percent of median income of the metropolitan area.

This proposed rule would codify the interpretation of ''underserved area'' provided in the Mortgagee Letter. Specifically, the proposed rule would amend § 202.3(c)(2) to specify that the term ''underserved area'' will have the same meaning as that provided in 24 CFR 81.2.

G. Informal Conference Prior to Termination

The regulations provide that prior to termination the mortgagee may request an informal conference with HUD. However, the regulations do not currently specify the timeframes for submission of such a request, nor for the holding of the informal conference. This proposed rule would specify that HUD must receive the written request for the informal conference no later than 30 calendar days after the date of the proposed termination notice. Unless HUD grants an extension, the informal conference must be held no later than 60 calendar days after the date of the proposed termination notice.

H. Reinstatement of Terminated Origination Approval Agreements

The proposed rule would also add a new § 202.3(e) describing the procedures a terminated mortgagee must follow to have its origination approval agreement reinstated. A mortgagee whose origination approval agreement has been terminated may apply for reinstatement if the origination approval agreement has been terminated for the affected branch or branches for at least six months and the mortgagee continues to be an approved mortgagee meeting the general standards of § 202.5 and the specific requirements of §§ 202.6, 202.7, 202.8 or 202.10, and 202.12.

The mortgagee's application for reinstatement must be accompanied by an independent analysis of the terminated office's operations and identifying the underlying cause of the mortgagee's unacceptable default and claim rate. The independent analysis must be prepared by an independent Certified Public Accountant (CPA) qualified to perform audits under the government auditing standards issued by the General Accounting Office. The application must also contain a corrective action plan addressing each of the issues identified in the CPA analysis and include evidence demonstrating that the mortgagee has implemented the corrective action plan. The Secretary will grant the mortgagee's application for reinstatement if the mortgagee's application is complete and the Secretary determines that the underlying causes for the termination have been satisfactorily remedied.

III. Small Business Concerns Related to Credit Watch Termination Initiative

With respect to termination of the mortgagee's Agreement, or taking other appropriate enforcement action against a mortgagee, HUD is cognizant that section 222 of the Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) (SBREFA) requires the Small Business and Agriculture Regulatory Enforcement Ombudsman to ''work with each agency with regulatory authority over small businesses to ensure that small business concerns that receive or are subject to an audit, on-site inspection, compliance assistance effort, or other enforcement related communication or contact by agency personnel are provided with a means to comment on the enforcement activity conducted by this personnel.'' To implement this statutory provision, the Small Business Administration has requested that agencies include the following language on agency publications and notices that are provided to small business concerns at the time the enforcement action is undertaken. The language is as follows:

> **Your Comments Are Important**
>
> The Small Business and Agriculture Regulatory Enforcement Ombudsman and 10 Regional Fairness Boards were established to receive comments from small businesses about federal agency enforcement actions. The Ombudsman will annually evaluate the enforcement activities and rate each agency's responsiveness to small business. If you wish to comment on the enforcement actions of [insert agency name], you will find the necessary comment forms at *http://www.sba.gov.ombudsman* or call 1–888–REG–FAIR (1–888–734–3247).

In accordance with its notice describing HUD's actions on the implementation of SBREFA, which was published on May 21, 1998 (63 FR 28214), HUD will work with the Small Business Administration to provide small entities with information on the Fairness Boards and National Ombudsman program, at the time enforcement actions are taken, to ensure that small entities have the full means to comment on the enforcement activity conducted by HUD.

IV. Findings and Certifications

Regulatory Planning and Review

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866, Regulatory Planning and Review. OMB determined that this proposed rule is a ''significant regulatory action'' as defined in section 3(f) of the Order (although not an economically significant regulatory action under the Order). Any changes

made to this rule as a result of that review are identified in the docket file, which is available for public inspection in the office of the Department's Rules Docket Clerk, Room 10276, 451 Seventh Street, SW., Washington, DC 20410–0500.

Regulatory Flexibility Act

The Secretary has reviewed this proposed rule before publication, and by approving it certifies, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), that this proposed rule would not have a significant economic impact on a substantial number of small entities. The reasons for HUD's determination are as follows.

This proposed rule would make several amendments to HUD's regulations for the FHA Credit Watch Termination Initiative. First, consistent with the goals of the Administration regarding the increased use of technology in government, the proposed rule would allow for a fully computerized Credit Watch notification process through use of the FHA Neighborhood Watch Early Warning System. This proposed change would provide for a streamlined and more effective method of monitoring mortgagee performance and for notifying poor performing mortgagees that are in danger of having their Agreements terminated by HUD. The change would not impose an undue burden on small entities, since it merely codifies existing HUD policy previously announced through a Mortgagee Letter. Further, the majority of mortgagees (small and large) participating in the FHA mortgage insurance programs currently have access to the FHA Internet Connection that is used to provide such notification.

The proposed rule would also remove the regulatory cap on the Credit Watch default and claim rates, and providing that a mortgagee will be considered to be on Credit Watch Status if it has a default and claim rate on insured mortgages that exceeds 150 percent of the normal rate and its Agreement has not been terminated. This revision would not impose a significant economic impact on small entities, since the entities that would be affected by this change are poor performing mortgagees that are already subject to termination of their Agreements.

The proposed rule also would prohibit a mortgagee that has received a notice of proposed termination of its Agreement from establishing a new branch for the origination of FHA-insured mortgages in the lending area covered by the proposed termination. The mortgagees to which this change would be applicable are those that already have been notified by HUD that their default and claim rates exceed an acceptable standard in specified geographic areas and they are at risk of having their FHA mortgage origination approvals terminated. The appropriate logical response to a notice of proposed termination is not to have this same mortgagee open a new branch in the same lending area before risks have been mitigated and problems corrected. The intent of this rulemaking is to close a loophole used by mortgagees to evade HUD's existing procedure for reviewing losses to the insurance funds.

The proposed rule would also establish that the default and claim thresholds underlying the Credit Watch Termination Initiative apply to both underwriting and originating mortgagees. This amendment will ensure that the performance of all mortgagees involved in FHA-insured mortgage transactions is evaluated. To the extent that the proposed change would have an economic impact on small underwriting mortgagees who are presently not covered by Credit Watch Termination, it will be as a result of actions taken by the mortgagees themselves—that is, failure to undertake the sound business practices necessary to maintain default and claim rates at an acceptable level.

The proposed rule would also provide that, for purposes of the Credit Watch Termination evaluation, the date of mortgage origination would be considered to be the date the loan transaction commences amortization, rather than the date of endorsement for FHA mortgage insurance as provided in the current regulation. This proposed change would not impose any economic burden on small mortgagees. Rather, the change would improve the accuracy of Credit Watch Termination evaluations by conforming HUD's definition of the mortgage origination date to the beginning amortization date used to report defaults. Finally, the proposed rule would codify existing definition of the term ''underserved area'' for purposes of Credit Watch Termination determinations. This proposed amendment would merely codify existing policy and would, therefore, not impose any new economic burden on mortgagees.

Notwithstanding HUD's determination that this rule will not have a significant economic effect on a substantial number of small entities, HUD specifically invites comments regarding any less burdensome alternatives to this rule that will meet HUD's objectives as described in this preamble.

Environmental Impact

This proposed rule would not direct, provide for assistance or loan and mortgage insurance for, or otherwise govern or regulate, real property acquisition, disposition, leasing, rehabilitation, alteration, demolition, or new construction, or establish, revise, or provide for standards for construction or construction materials, manufactured housing, or occupancy. Accordingly, under 24 CFR 50.19(c), this proposed rule is categorically excluded from the requirements of the National Environmental Policy Act (42 U.S.C. 4332 *et seq.*).

Executive Order 13132, Federalism

Executive Order 13132 (entitled ''Federalism'') prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial direct compliance costs on state and local governments and is not required by statute, or the rule preempts state law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This proposed rule would not have federalism implications and would not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) establishes requirements for federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments, and on the private sector. This proposed rule would not impose any federal mandates on any state, local, or tribal governments, or on the private sector, within the meaning of the Unfunded Mandates Reform Act of 1995.

Catalog of Federal Domestic Assistance

The Catalog of Federal Domestic Assistance Program number applicable to 24 CFR part 202 is 14.20.

List of Subjects in 24 CFR Part 202

Administrative practice and procedure, Home improvement, manufactured homes, Mortgage insurance, Reporting and recordkeeping requirements.

Accordingly, for the reasons described in the preamble, HUD proposes to amend 24 CFR part 202 as follows:

PART 202—APPROVAL OF LENDING INSTITUTIONS AND MORTGAGEES

1. The authority citation for 24 CFR part 202 continues to read as follows:

Authority: 12 U.S.C. 1703, 1709, and 1715b; 42 U.S.C. 3535(d).

2. Amend § 202.3 by revising paragraph (c)(2) and adding paragraph (e) to read as follows:

§ 202.3 Approval status for lenders and mortgagees.

* * * * *

(c) * * *

(2) *Termination of the origination approval agreement.* (i) *Scope and frequency of review.* The Secretary will review, on an ongoing basis, the number of defaults and claims on mortgages originated, underwritten, or both, by each mortgagee in the geographic area served by a HUD field office. HUD will make this rate information available to mortgagees and the public through electronic means and will issue instructions for accessing this information through a Mortgagee Letter. For this purpose, and for all purposes under paragraph (c) of this section, a mortgage is considered to be originated in the same federal fiscal year in which its amortization commences. The Secretary may also review the insured mortgage performance of a mortgagee's branch offices individually and may terminate the authority of the branch or the authority of the mortgagee's overall operation.

(ii) *Credit Watch Status.* Mortgagees are responsible for monitoring their default and claim rate performance. A mortgagee is considered to be on Credit Watch Status if, at any time, the mortgagee has a rate of defaults and claims on insured mortgages originated, underwritten, or both, in an area which exceeds 150 percent of the normal rate and its origination approval agreement has not been terminated. A poor performing mortgagee on Credit Watch Status is in danger of having its origination approval agreement terminated by HUD.

(iii) *Effect of default and claim rate determination.* (A) The Secretary may notify a mortgagee that its origination approval agreement will terminate 60 days after notice is given, if the mortgagee had a rate of defaults and claims on insured mortgages originated, underwritten, or both, in an area which exceeded 200 percent of the normal rate and exceeded the national default and claim rate for insured mortgages. The termination notice may be given without prior action by the Mortgagee Review Board.

(B) Before the Secretary sends the termination notice, the Secretary shall review the Census tract concentrations of the defaults and claims. If the Secretary determines that the excessive rate is the result of mortgage lending in underserved areas, as defined in 24 CFR 81.2, the Secretary may determine not to terminate the origination approval agreement.

(C) Prior to termination the mortgagee may submit a written request for an informal conference with the Deputy Assistant Secretary for Single Family Housing or that official's designee. HUD must receive the written request no later than 30 calendar days after the date of the proposed termination notice. Unless HUD grants an extension, the informal conference must be held no later than 60 calendar days after the date of the proposed termination notice. After considering relevant reasons and factors beyond the mortgagee's control that contributed to the excessive default and claim rates, the Deputy Assistant Secretary for Single Family Housing or designee may withdraw the termination notice.

(D) Upon receipt of a proposed termination notice, the mortgagee shall not establish a new branch or new branches for the origination of FHA-insured mortgages in the area or areas that are covered by the proposed termination notice. As of [effective date of final rule to be inserted at final rule stage] a mortgagee that is in receipt of a notice of proposed termination may not establish any new branch in the location or locations cited in the proposed termination notice until either:

(1) The proposed termination notice is rescinded; or

(2) The Secretary reinstates the mortgagee's origination approval agreement, in accordance with paragraph (e) of this section.

(iv) *Rights and obligations in the event of termination.* If a mortgagee's origination approval agreement is terminated, it may not originate or underwrite single family insured mortgages unless the origination approval agreement is reinstated by the Secretary in accordance with paragraph (e) of this section, notwithstanding any other provision of this part except § 202.3(c)(2)(iv)(A). Termination of the origination approval agreement shall not affect:

(A) The eligibility of the mortgage for insurance, absent fraud or misrepresentation, if the mortgagor and all terms and conditions of the mortgage had been approved before the termination by the Direct Endorsement or Lender Insurance mortgagee or were covered by a firm commitment issued by the Secretary; however, no other mortgages originated by the mortgagee shall be insured unless a new origination approval agreement is accepted by the Secretary;

(B) A mortgagee's obligation to continue to pay insurance premiums and meet all other obligations, including servicing, associated with insured mortgages;

(C) A mortgagee's right to apply for reinstatement of the origination approval agreement in accordance with paragraph (e) of this section; or

(D) A mortgagee's right to purchase insured mortgages or to service its own portfolio or the portfolios of other mortgagees with which it has a servicing contract.

* * * * *

(e) *Reinstatement of terminated origination approval agreement.* (1) *Reinstatement.* A mortgagee whose origination approval agreement has been terminated under paragraph (c) of this section may apply for reinstatement if:

(i) The origination approval agreement for the affected branch or branches has been terminated for at least six months; and

(ii) The mortgagee continues to be an approved mortgagee meeting the general standards of § 202.5 and the specific requirements of §§ 202.6, 202.7, 202.8 or 202.10, and 202.12.

(2) *Application for reinstatement.* The mortgagee's application for reinstatement must:

(i) Be in a format prescribed by the Secretary and signed by the mortgagee;

(ii) Be accompanied by an independent analysis of the terminated office's operations and identifying the underlying cause of the mortgagee's unacceptable default and claim rate. The independent analysis must be prepared by an independent Certified Public Accountant (CPA) qualified to perform audits under the government auditing standards issued by the General Accounting Office; and

(iii) Be accompanied by a corrective action plan addressing each of the issues identified in the independent analysis described in paragraph (e)(2)(ii) of this section, along with evidence demonstrating that the mortgagee has implemented the corrective action plan.

(3) *HUD action on reinstatement application.* The Secretary will grant the mortgagee's application for reinstatement if the mortgagee's application is complete and the Secretary determines that the underlying causes for the termination have been satisfactorily remedied.

Dated: March 2, 2003.

John C. Weicher,

Assistant Secretary for Housing-Federal Housing Commissioner.

[FR Doc. 03–7704 Filed 3–31–03; 8:45 am]

BILLING CODE 4210–27–P