

Congress Raises FHA Borrower Cash Requirements

[On behalf of Dornish Law Offices, PC](#) | Oct 1, 2008 | [All, Real Estate Practice](#)

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On July 31, 2008, changes to Paragraph (9) of section 203(b) of the National Housing Act (12 U.S.C. 1709(b)(9)) went into effect. In short, the amendments lay out cash investment requirements for buyers, and what sources of such buyers' funds are permitted in order for the mortgage to be insured. The new restrictions prohibit all types of seller-funded down payment assistance.

In subparagraph (A) of 12 U.S.C. 1709(b)(9), a borrower must pay at least 3.5% of the appraised value of the property in cash or its equivalent in order for a loan to be insured under the section. The 3.5% down payment requirement is an amendment increasing the minimum from 3.0%.

The funds which can be used to satisfy the 3.5% requirement from subparagraph (A) are not allowed to come from certain prohibited sources, which are indicated in subparagraph (C). In subparagraph (C), it states that **in no case** can funds, either in whole or in part, come from "(i) [t]he seller or any other person or entity that financially benefits from the transaction" or from "(ii) [a]ny third party or entity that is reimbursed, directly or indirectly, by any of the parties described in clause (i)." These indicated sources are prohibited before, during or after the closing of the property, and applies only to mortgages with a credit approval from a lender on or after October 1, 2008.

The types of down payment assistance which are specifically targeted by these new regulations include seller assistance at closing, which is effectively limited by these regulatory changes to 1.5% in low 5% down payment federally insured loans. However, they also target programs like Ameridream, where sellers paid a third party a fee, and the third party provided down payment assistance to borrowers.

However, as of October 2, 2008, there has already been proposed legislation to revise these newly enacted requirements for seller-financed down payments. (*See* H.R. 6694, Report No. 110-905). The proposed

changes would change the language in subparagraph (C) from stating “in no case” to “except in the case of a mortgage described in subparagraph (D),” adding a separate provision that lists exceptions to the prohibited sources. There are two proposed exceptions: one for a borrower having a FICO score of 680 or greater and the other dealing with a borrower who has a FICO of at least 620 but less than 680 and who can meet an extra list of requirements dealing with the mortgage insurance premiums charged. The proposed bill would also include requirements for down payment assistance entities and a section dealing with civil money penalties for improperly influencing appraisals.

It is evident that more changes are likely to be implemented in the near future regarding appropriate sources of down payments on FHA loans, creating uncertainty in the meantime as to when and under what circumstances seller-financed down payment options may soon again exist. However, the only safe way to proceed on any down payment assistance in this ever changing sea of regulations is to make sure as a buyer or seller, that the amount and source of any down payment assistance is fully disclosed on the HUD -1 settlement sheet, and that the settlement sheet is signed exactly as it has been pre-approved by the lender.

Any time you are asked to make or receive down payment assistance not shown on the settlement sheet, know that you are likely being asked to do so to avoid disclosing something which violates applicable regulations or lender requirements. If you sign a HUD-1 which does not accurately reflect the whole transaction, including seller assistance to the buyer, you are violating the representation on the HUD form itself, and with it Federal law. Although Federal Prisons are supposedly very nice, I for one never want to find out how nice they are. I'd rather not buy or sell a property, than to close the transaction fraudulently, in violation of the law.

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