



## MEMORANDUM

May 6, 2019

To: Housing Clients

From: HOBBS, STRAUS, DEAN & WALKER, LLP

Re: *Draft of Section 184 Loan Guarantee Regulations for Tribal Comment*

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### *I. Introduction*

As we previously reported, on April 4, 2019, the Department of Housing and Urban Development's Office of Native American Programs (HUD ONAP) issued a "Dear Tribal Leader" letter and the new set of Section 184 draft regulations (attached) to replace the existing regulations at 24 CFR Part 1005. This draft is still the Tribal consultation draft. The regulations will go through another round of Tribal comments and consultation before HUD publishes a draft version for public comment in the Federal Register. This memo provides a detailed summary of the provisions in the new regulations. **Comments are due on June 3, 2019.** Comments on the proposed rule can be submitted by email to: [184consultation@hud.gov](mailto:184consultation@hud.gov). Alternatively, Tribes may submit comments by postal mail to:

Krisa Johnson, Director, Office of Loan Grantee  
HUD – Office of Native American Programs  
451 Seventh Street SW, Room 4108  
Washington, D.C. 20410.

Additionally, HUD will be holding a tribal consultation session about the draft proposed rule on Wednesday, May 8, 2019 from 1:45 pm to 3:15 pm at the Denver Convention Center. The consultation will be held in conjunction with the National American Indian Housing Council (NAIHC) annual meeting; however, one does not have to register for the NAIHC annual meeting to attend the consultation session.

As HUD describes it, the purpose of developing new Section 184 regulations is the significant growth of the program since its inception in 1994: from fewer than 100 loans in 1994, to more than 4,000 loans worth over \$700 million in fiscal year 2017. Yet despite that growth, the regulatory framework that governs the program has remained largely unchanged. The initial regulations are very short, and do not provide a lot of detail. The initial HUD consultation notice states: "Given the growth and maturity of the program, HUD finds it necessary to expand and revise the regulations to meet the program's growing demands, and to hold participating banks accountable to both tribes and the federal government." The draft regulations contain 141 pages of text.

## ***II. Summary of Draft Regulations***

Here is a section-by-section summary of the main points of the draft regulations, with commentary where appropriate.

### **A – General Program Requirements**

This section sets out the purposes of the Section 184 program: to provide loan guarantees to tribes, TDHEs, or individual tribal members and families for the purposes of obtaining financing to construct, acquire, refinance or rehabilitate one- to four-family housing located on or off tribal lands.

### **B – Financial Institution Eligibility & Requirements**

One of the issues the new regulations try to address is the ongoing difficulty in getting banks and other lenders to participate in the Section 184 program, which includes a fairly cumbersome lender-approval process. This section provides the details for eligibility and approval, some of which are carried over from the existing regulation, and others which provide more options for lenders:

- As in the current regulation, several types of financial institutions are deemed “approved” by the regulation, including lenders already approved under several other statutory programs: HUD Title II (single-family mortgage program); HUD Housing loans under 38 U.S.C. § 3702(d); USDA guaranteed loan program; Community development financial institutions (CDFIs).
- Other lenders can submit applications to be approved, and must meet the requirements set out in this subpart, including having at least five years’ experience, or having a principal officer with five years’ experience.
- Direct lenders can also sponsor other non-direct guarantee lenders, and provide underwriting, closing, and servicing of Section 184 guaranteed loans.
- Lenders must adopt quality control plans to ensure the quality of their origination, underwriting, closing, endorsement, and servicing and minimize risk, and submit those plans to HUD or the relevant approving federal agency.
- Direct guarantee lenders and sponsored non-direct guarantee lenders must actively market, originate, underwrite, close, and service a minimum amount of loans on trust land.

## C – Tribal Participation

The Section 184 program was initially developed to spur lending on reservation lands, where it was difficult to involve private lenders due to the non-alienable status of trust land. The program was expanded during the 2000s to include non-trust lands, and it has been more successful in that area than on-reservation. Some of the language in Subpart C appears to be aimed at encouraging more on-reservation lending.

- To participate, a tribe must show that tribal legal and administrative structures exist to protect the interests of the borrower, the lender and HUD, and that address defaults by the borrower. *These include foreclosure ordinances processed through “legal systems having jurisdiction over the Section 184 loans.”* (This language leaves open a significant issue raised in the past few years by HUD/DOJ, stating that they could not approve loans that would be enforced in Tribal Court – and this language is less clear about Tribal Court jurisdiction than the current regulations).
- The ordinance must provide the tribe with the option of reassigning the loan to HUD, and create eviction procedures that enable the lender, TDHE or HUD to take possession of the property in the event of reassignment of the lease, or if the lease is vacated.
- The tribal ordinance must also ensure that Section 184 loans hold a first lien position or apply state law to determine the lien position.
- The Tribe must grant access to HUD and participating lenders to tribal lands in order to service and evaluate properties guaranteed under Section 184 loans, have effective foreclosure and eviction procedures that the tribe consistently enforces.
- In the event these provisions or tribal enforcement of them is lacking, HUD can cease guaranteeing new Section 184 loans in the Tribe’s area, give HUD first lien priority to the property, or otherwise ensure the Section 184 loan will be satisfied before all other property debts.

## D – Underwriting

One of the other concerns with the Section 184 program was the timeliness of HUD’s underwriting. This subpart sets out more detail on what such underwriting will involve (some of which are to prevent use of the program as a means of speculating in real estate). Whether providing more detail is sufficient, or whether it will expedite the process, is an open question.

- Eligible borrowers include Indian families, Indian tribes, and TDHEs.

- Family borrowers must occupy the dwelling as their principal residence, but may have a co-borrower that does not occupy the residence if the co-borrower is family by blood or other longstanding and substantial relationship.
- Borrowers may be rated on their gross income, credit standing, previous foreclosure on HUD guaranteed property, verification of Social Security, Employer or Tax Identification Numbers, and whether the borrower is the owner of record (rather than by sale or assignment of the sales contract).
- In addition to requiring the property be purchased from the owner of record, there are restrictions on how soon a property can be re-sold. Properties changing ownership (re-sale following acquisition by the seller) within 90 days are not eligible for the Section 184 program. Between 91 and 180 days the resold properties are generally eligible with additional documentation, and up to 12 months, some additional documentation may be required if the re-sale price is greater than 5% higher than the purchase price. If the re-sale occurs more than 12 months from the acquisition of the property to be financed by the Section 184 guaranteed loan, the property is eligible. These restrictions do not apply to tribes, TDHEs, Indian Housing Authorities, or state and local governments.

### **E – Closing and Endorsement**

Again, this section seeks to provide substantially more detail on the process for closing and endorsement, with the aspiration of making the process more efficient, and also to protect borrowers from predatory lending. Among the major provisions included are the following:

- For trust properties, the lender must follow guidance from HUD to prove chain of ownership. All properties must have all objections to binder/initial certified title status reports cleared and assurance that the guaranteed loan will be in the first lien position.
- Lender must ensure the borrower executes a third-party notification form to the tribe at closing.
- The guaranteed loans must have monthly payments equal to one-twelfth of the annual loan guarantee premium payable by the lender to HUD in conformance with the amortization schedule issued with the loan approval.
- The borrower must be permitted to prepay the loan in whole or in part without any prepayment fees.
- The loan must provide a sufficient amortized amount to cover ground rents, Section 184 loan guarantee fees, estimated amount of all taxes, special assessments, and insurance premiums. The lender must pay those costs before

any delinquencies, all costs for premiums and any other fees which protect only the lender.

- The lender may collect only certain fees from the borrower to cover their actual costs, and all such fees and charges must be disclosed and approved by HUD before the issuance of a loan guarantee.
- *Endorsement.* The lender must complete a pre-endorsement review of the endorsement file by staff not involved in the originating, processing, or underwriting of the loan. HUD will then review the documents and issue a loan guarantee certificate if it meets all statutory and regulatory requirements, and includes no false, misleading, fraudulent information or misrepresentation is included in the documents.
- HUD may also conduct post-endorsement reviews, and even cancel a previously issued loan guarantee certificate.
- The originating lender shall indemnify HUD for any underwriting deficiencies that would have disqualified the loan guarantee from being issued in the first place.
- In general, a loan guarantee certificate evidences HUD's review determination that the lender's pre-endorsement case file complies with Section 184 statutory and regulatory requirements. The loan guarantee certificate is conclusive evidence of the loan's Section 184 eligibility, however it does not prevent HUD from establishing defenses against the original lender based on fraud, material misrepresentation, or partial defenses to the amount payable to the guarantee.

#### **F – Section 184 Loan Guarantee Fees**

HUD charges the borrower a one-time up-front loan guarantee fee and an annual loan guarantee fee, to be collected by the lender on behalf of HUD and payable in cash.

- The lender will collect the one-time fee at settlement, and the one-time fee is determined by HUD as a percentage of the base loan amount. The lender will collect the annual loan guarantee fee in monthly installments, due to HUD by the tenth day of each month.
- The lender may not pass the cost of any penalties imposed by HUD on to the borrower. Such penalties include failure to remit up-front loan guarantee fees within 15 days of settlement, failure to submit the monthly installment of the annual loan, to adjust the annual loan guarantee fee, and continuing to collect the annual loan guarantee fee after its value ratio reaches the threshold in Section 1005.607(d). In the last scenario, the lender must reimburse the borrower and pay HUD a penalty for each month of over-collection.

## G – Loan Servicing

This section sets out the requirements for lenders who service the Section 184 guaranteed loans, as well as the sanctions for failure to comply. The requirements include:

- Must comply with the Real Estate Settlement Procedures Act (12 U.S.C. § 2601 *et seq.*) and the Truth in Lending Act (15 U.S.C. § 1601 *et seq.*) at 12 CFR Part 1024 and 12 CFR Part 1026.
- If the servicing of a loan is transferred from one servicer to another, notice must be given in accordance with 12 CFR § 1024.33, and include partial payment requirements described below (*see* draft Sec. 1005.719).
- Servicers must provide loan information to borrowers and provide individual loan consultation on request, and must also provide the borrower with a statement of interest paid and taxes disbursed from escrow annually.
- *Assumption.* Guaranteed loans are fully assumable by an eligible borrower, determined to be creditworthy by the servicer for direct guarantee loans, and as determined by HUD for other loans. If the property is on tribal trust lands, the lease document may require tribal and Bureau of Indian Affairs (BIA) approval of the assignment of the lease to the new borrower. Upon assumption the servicer must release the original borrower from all liability. Servicers may not impose or agree to legal restrictions on conveyances or assumptions of the guaranteed loan, unless an exception applies.
- In general, all Section 184 loans must include a due-on-sale clause allowing for acceleration of the loan. If a sale or transfer occurs without the servicer's approval in contradiction of this section, the servicer shall enforce the loan acceleration with approval from HUD, provided acceleration is otherwise legal.
- *Late charges.* The servicer must have a publicly available, written policy on partial payments. The servicer must accept prepayments at any time and in any amount, and apply them to the balance on the date received. Borrowers may be substituted as a co-borrower for the original borrower by HUD only if the co-borrower is also eligible and a remaining original borrower is still on the loan.
- *Servicing Loan Default.* Loan defaults shall be reported in the manner HUD establishes through administrative guidance. Before the servicer can seek payment from HUD for a guaranteed loan, they must promptly collect overdue amounts from borrowers or exhaust all reasonable collection actions and offer loss mitigation to eligible borrowers. The servicer must promptly make live

contact with the borrower and inform them of loss mitigation options. The servicer must make good faith efforts to contact the borrower.

- *Notice requirements.* The servicer must give written notice to a borrower in default on a HUD-approved form by the 45<sup>th</sup> day of the default. The servicer must comply with the loss mitigation application timeline and appeals process.
- *Loss Mitigation Program.* The purpose of loss mitigation is to cure the borrower's default and minimize any financial loss to HUD, and the servicer must comply with 12 CFR Part 1024 in carrying it out. Special options exist for borrowers in military service, including postponement of principal payments, and postponement of foreclosure. The servicer may advance incentive payments to the borrower for completing loss mitigation options with HUD approval.
- *Forbearance* – Both informal and formal forbearance plans in lieu of foreclosure are permitted. The proposed regulation sets out a number of requirements for such plans.
- *Loan modification* – Loan modifications are permitted, but with specific conditions. Before modifying a loan, the servicer must ensure the borrower can support the monthly debt after the loan modification. In addition to borrower eligibility, the servicer must also consider and ensure the condition of the property, if the servicer reasonably believes the property's condition will adversely impact the borrower's use or ability to support the debt. The borrower may have the option of a trial payment plan as part of the loan modification, which is a written agreement executed by all parties on the original note and the guaranteed loan for a minimum of three (3) months.
- After borrower fails a trial payment plan, the servicer must offer deed-in-lieu or lease-in-lieu, and any submitted payments must be applied to any shortages or reduce the amount to be capitalized on the principal balance.
- *Pre-foreclosure sales ("short sales")* – Short sales are permitted, but with certain conditions and with HUD approval. The servicer must calculate the borrower's cash reserves and require their contribution before executing the pre-foreclosure sale, ensure good and marketable title, notify all junior lien holders of the potential short sale, and ensure property is properly valued. Servicer must also send a right of first refusal to the tribe and the TDHE, and review the marketing status of the property every month. The borrower must wait 15 days to accept an offer, with the maximum marketing period lasting four (4) months, unless the property is under contract, which provides a two-month extension.
- *Deed-in-lieu / Lease-in-lieu* – Instead of instituting foreclosure, the servicer may acquire the property through voluntary conveyance from the borrower, subject to

tribal, BIA and HUD approval, along with conditions set out in the draft regulation.

- *Foreclosure or Assignment of the Mortgage to HUD.* If the loss mitigation options have not been used, the servicer must initiate foreclosure for fee simple properties insured under the Section 184 program. For tribal trust lands, the servicer may still initiate foreclosure, or it may assign the loan to HUD with the agency's approval. The servicer may also assign the mortgage to HUD between 120-180 days after the default if certain conditions are met: (1) servicer has reviewed borrower's loss mitigation request and determined they do not qualify and rejected any appeal by the borrower, (2) the borrower failed to perform under a loss mitigation option, or (3) the borrower is unresponsive to servicer's inquiries.

## **H – Claims**

This section addresses the steps a lender must take to make a claim for payment under the loan guarantee.

- There are five claim types, including conveyance, assignment of the loan, post-foreclosure claims without conveyance of title, pre-foreclosure sale, and supplemental claims.
- The lender may submit a Part A claim for unpaid principal balance, or a Part B claim, which is for interest on unpaid principal balance.
- HUD may review a claim file at any time, and a lender's denial of HUD's access to a file may be grounds for withdrawal of the lender's approved status or immediate suspension of all claim payments. If HUD finds violations of the regulatory requirements by the lender, it may deny the claim, demand reimbursement of all claim amounts, expenses paid, demand reconveyance of the property cancel the loan guarantee certificate, and/or pursue sanctions against the originating lender.
- All property title transfers from the lender must be conveyances of good and marketable title and transfers of possession of the property. Lenders may provide satisfactory title evidence to HUD by submitting fee or owner's title policy, lender's policy of title insurance, abstract and legal opinion, a Torrens or similar title certificate, title standard of U.S., tribal or state government, or certified title status report issued by the BIA.
- HUD will not object to title restrictions placed on the tract of tribal trust land by the tribe or by the BIA. HUD will use industry standards to verify sufficient evidence of good title, but ultimately will make the final decision.



- HUD reserves the right to post-claim payment review for up to five years. Once HUD makes its final payment to the lender or servicer, they will have no further claims against the borrower or HUD. However, HUD may still seek reimbursement of costs and return amounts from the lender.
- HUD may also seek reimbursement from noncompliant servicers of all claim and carrying costs. If HUD reconveys a property back to a lender, HUD will not seek reimbursement from them, but will seek reimbursement of costs from servicer.

### **I – Lender Monitoring, Reporting, Sanctions, and Appeals**

This section sets out HUD’s compliance and sanctions framework for non-compliant lenders.

- HUD will periodically review lenders and conduct on-site monitoring to evaluate the lender’s compliance with the Section 184 regulations, and propose corrective actions if necessary.
- The lenders and servicers must provide timely and accurate reports, and may be required to report more often if HUD identifies deficiencies, or even be subject to sanctions and civil money penalties.
- HUD may use sanctions against a lender when that lender fails to maintain adequate accounting records, adequately service loans, use proper credit or underwriting judgment, is ineligible to participate, or has engaged in detrimental practices harming the interest of the borrower or the United States.
- Sanctions include: (1) refusal to guarantee or service, temporarily or permanently, any loans made by the lender, (2) bar lender from acquiring additional loans, (3) require the lender to assume at least 10 percent of any loss on further loans, (4) require the lender comply with a corrective action plan or amend their quality control plan, as approved by HUD.
- Additionally, HUD may impose civil money penalties for these same deficiencies as authorized under Section 356 of the National Housing Act (12 U.S.C. § 1735f-4).

*Again, the comment period ends on June 3, 2019. Please let us know if you would like assistance in drafting comments.*

If you have any questions about the items in this memorandum, please do not hesitate to contact Edmund Clay Goodman at [egoodman@hobbsstrauss.com](mailto:egoodman@hobbsstrauss.com) or by phone at (503) 242-1745.