FannieMae
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Announcement 07-25 ***December 21, 2007***

Amends these Guides: Selling and Servicing

Expansion of Eligibility for Inter Vivos Revocable Trusts; Update to Flood Insurance Coverage Requirements for Mortgages Secured by One-Family to Four-Family Properties; Use of Automated Valuation Models (AVMs) to Support the Cancellation of Mortgage Insurance (MI) Coverage; Update to Policy for Postponed Improvements; Clarification of the Appraisal Requirements for Manually Underwritten Mortgages; and Delinquency Status Reporting for Regular Servicing Option Loans

Introduction

This Announcement addresses five Fannie Mae Selling and/or Servicing Guide topics to update and/or clarify existing requirements, and communicate new requirements, as itemized below:

- Expansion of the eligibility parameters to include 2-family to 4-family principal residence and investment properties when the borrower is an *inter vivos* revocable trust;
- Update to the flood insurance coverage requirements for mortgages secured by one-family to four-family properties;
- Clarification that the value provided by an Automated Valuation Model (AVM) may not be used to support cancellation of mortgage insurance (MI) coverage;
- Update to the policy for postponed improvements; and
- Clarification of the appraisal requirements for manually underwritten mortgages;
- New requirements for servicers on reporting delinquency status for regular servicing option loans.

Expansion of Eligibility for *Inter Vivos* Revocable Trusts

Selling Guide Part IV, Section 501, Documentation for Mortgages to Inter Vivos Revocable Trust Borrowers, and Part VII, Section 101.06, Inter Vivos Revocable Trusts.
Fannie Mae currently accepts an *inter vivos* revocable trust as an eligible borrower for a conventional first mortgage that is secured by a one-family principal residence, second home, or an investment property, provided the trust complies with the eligibility requirements stated in the *Guide*. In addition, *Selling Guide* Part I, Section 202.01, Additional Selling Warranties requires the lender to provide a specific representation and warranty that holding title to the property in a trust does not in any way diminish Fannie Mae's rights as a creditor, including the right to have full title to the property vested in Fannie Mae should foreclosure proceedings be initiated under the terms of the mortgage.

We are expanding our policy to permit *inter vivos* revocable trusts as an eligible borrower for conventional first mortgage loans secured by one-family to four-family principal residences, investment properties, and one-family second homes. In addition, we are clarifying that eligible properties include units in condominium projects, planned unit developments (PUDs), manufactured homes and cooperatives (provided the lender has obtained approval to deliver cooperatives to Fannie Mae) that comply with our existing requirements.

Change to Flood Insurance Coverage Requirements for Mortgages Secured by One-Family to Four-Family Properties

Selling Guide Part V, Section 403, Coverage for First Mortgages.
Fannie Mae is revising its minimum flood insurance requirements for mortgages secured by one-family to four-family properties. Currently, Fannie Mae requires the minimum amount of coverage to equal 80 percent of the replacement cost of the dwelling when the unpaid principal balance is the lowest option. With this Announcement, Fannie Mae is changing the requirement for coverage to be the lowest of:

- 100 percent of the replacement cost of the dwelling;
- The maximum insurance available under the National Flood Insurance Program; or
- The unpaid principal balance of the mortgage.

Use of Automated Valuation Models (AVMs) to Support the Cancellation of Mortgage Insurance (MI) Coverage

Servicing Guide Part II, Section 102.05 Borrower-Initiated Cancellation Based on Current Property Value.
Fannie Mae has received several inquiries related to the use of an Automated Valuation Model (AVM) to establish the current property value to support cancellation of mortgage insurance (MI) coverage. As stated in the *Guide*, a borrower is allowed to request cancellation of borrower-purchased MI coverage for any conventional mortgage, regardless of closing date, when that loan reaches a specified loan-to-value ratio. But the Guide requires that value be established by a current appraisal based on an interior/exterior property inspection.

For certain mortgage loans, Fannie Mae allows cancellation of MI coverage based on the current appraised value if the mortgage loan and the borrower meet stated conditions. The use of an appraisal provides a real time analysis of market activity, including a physical inspection of the subject property, to arrive at an accurate valuation. However, an AVM, relies on public record information to determine estimated value without any assessment of the current condition of the property. As such, Fannie Mae will not permit the cancellation of MI coverage based on the estimated value provided by an AVM, since a real estate appraisal completed by a qualified appraiser is the most appropriate standard and most reliable indicator for determining property value.

Update to Policy for Postponed Improvements

Selling Guide Part XI, Section 202 Status of Construction.
Generally, Fannie Mae requires that improvements to a property be complete when the mortgage is delivered to us. We do, however, permit the delivery of a mortgage loan prior to the completion of improvements (referred to as "postponed improvements") under certain circumstances in accordance with the *Guide*. We are making the following changes to our standard policies for postponed improvements for new or proposed construction as follows:

- The postponed improvements are no longer required to be "minor" conditions that do not affect the livability of the property; but they may be any condition that does not affect the livability of the property and the borrower's ability to obtain a certificate of occupancy from the applicable government authority.
- The terms of the postponed improvements must continue to be included as part of the sales contract for the property. However, third-party contracts are not acceptable.
- The cost of completing any improvements may not represent more than 10 percent of the "as completed" appraised value of the property (currently, this is limited to 2 percent).
- The mortgage and title insurance may not be impaired or adversely affected during or after the time the completion escrow is in effect.

Attachment 1 includes a revised *Selling Guide* Part XI, Section 202 that replaces the existing *Section* and reflects the changes noted above.

Clarification of the Appraisal Requirements for Manually Underwritten Mortgages

Selling Guide Part XI, Section 203 Appraisal and Property Inspection Forms.
Currently the *Guide* makes the following statement regarding our appraisal requirements:

"We have one appraisal report form for reporting an appraisal for each property and inspection type for both *Desktop Underwriter* and manually processed mortgages. The appraisal report form that should be used generally depends on the type of property and property inspection required."

With this Announcement, we are clarifying that all manually underwritten mortgages sold to Fannie Mae require an appraisal based on an interior and exterior property inspection and must be completed on the appropriate form depending on the property type, unless the specific product guidelines permit a less than full appraisal. As such, the following forms must be used for manually underwritten mortgages delivered to Fannie Mae, as applicable:

- *Uniform Residential Appraisal Report* (Form 1004);
- *Manufactured Home Appraisal Report* (Form 1004C);
- *Individual Condominium Unit Appraisal Report* (Form 1073);
- *Individual Cooperative Interest Appraisal Report* (Form 2090); and
- *Small Residential Income Property Appraisal Report* (Form 1025).

Lenders may download the appropriate form from eFannieMae.com or obtain the form through their forms vendor.

Delinquency Status Reporting for Regular Servicing Option Loans

Servicing Guide Part VII, Chapter 6: Delinquency Status Reporting.
Currently the reporting of delinquency status information for regular servicing option MBS pool mortgage loans is optional for servicers. Delinquency status information is needed, however, to adequately track delinquency data, as well as assist in compliance with our MBS Trust Agreements.

Effective March 1, 2008, servicers are required to report delinquency status information on any regular servicing option MBS pool mortgage loan that was three or more full payments (90 or more days) past due as of the last day of the preceding month until the loan becomes current. By the second business day of each month, a servicer must report (i) the specific "delinquency status" code that best describes the latest action it has taken to cure a delinquency or liquidate the mortgage, (ii) the effective date of the delinquency status that is being reported to us, and (iii) the specific "reason for delinquency" code that best describes the primary reason for a delinquency as part of its next scheduled delinquency status report

Descriptions of the available "delinquency status" codes and "reason for delinquency" codes appear in our *Servicing Guide* Part VII, Chapter 6, Exhibits 1 and 2. Each month, a servicer must electronically transmit a file extract of its delinquent mortgages to us, which Fannie Mae will then use to update its delinquency tracking system. For details of the flat file layout, refer to Announcement 07-03(R)2, Introduction of the Fannie Mae Single-Family MBS Master Trust Agreement (Supersedes Announcement 06-27), (Attachment 4) issued on August 17, 2007.

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Lenders who have questions about topics addressed in Announcement 07-25 should contact their Customer Account Team. For questions pertaining to any of the servicing-related topics, servicers should contact our National Servicing Organization's Customer Care Support Center at 1-888-326-6438 (option 2 – Servicing, then option 3 – General Servicing).

Michael A. Quinn
Senior Vice President
Single-Family Risk Officer

Attchment

Attachment 1

XI, Section 202: Status of Construction

Generally, we require improvements for the subject property to have been completed when the mortgage is delivered to us. (For specific information concerning manufactured homes, refer to *Part VII, Section 102.07.*) However, Fannie Mae does make some exceptions to this requirement for properties other than manufactured homes, and in such cases, an appraisal report should be developed in accordance with the following criteria:

- **New or proposed construction.** An appraisal may be based on either plans and specifications or an existing model home, if the lender obtains a certification of completion before it delivers the mortgage to us. This certification should be completed by the appraiser, state that the improvements were completed in accordance with the requirements and conditions in the original appraisal report, and be accompanied by photographs of the completed improvements.

  When the completion of certain improvements that are included as part of the sales contract (third party contracts are not permissible) that do not affect the ability to obtain an occupancy permit have been postponed for a valid reason, such as inclement weather or a shortage of building materials, the lender may deliver the mortgage before these postponed improvements are completed. These improvements include swimming pools, landscaping, driveways, etc. The lender represents and warrants that the postponed improvements will be completed within 180 days after the date of the mortgage note. The cost of completing any improvements must not represent more than 10 percent of the "as completed" appraised value of the property.

  - The lender must establish a "completion escrow" for postponed improvements, by withholding from the purchase proceeds funds equal to 120 percent of the estimated cost for completing the improvements. The mortgage insurance and title insurance may not be impaired or adversely affected during or after the time the completion escrow is in effect.

  - The lender and the borrower must enter into an escrow agreement that determines how the lender will manage and disburse funds from the escrow account. Once a certificate of completion is obtained, the lender must release the final draw from the escrow account (which should include any funds in excess of the amount needed to pay for completion of the postponed items). The final title report must not show any outstanding mechanic's liens or take any exceptions to the postponed improvements or the escrow agreement. If the final title report is issued before the completion of the improvements, the lender must obtain an endorsement to the title policy that ensures the priority of our lien.

- **Existing construction**. An appraisal may be based on the "as is" condition of the property if minor conditions that do not affect the livability of the property exist – such as minor deferred maintenance – as long as the appraiser's opinion of value reflects the existence of these conditions. For a property appraised in an “as is” condition, the lender must carefully review the appraisal to ensure that the property does not have any physical deficiencies or conditions that would affect its livability. If there are none, the lender does not need to require minor repairs to be completed before it delivers the mortgage to Fannie Mae.

When there are incomplete improvements or conditions that do affect the livability of the property – such as a partially completed addition or renovation – or physical deficiencies that could affect the soundness or structural integrity of the improvements, the property must be appraised subject to completion of the specific alterations or repairs. In such cases, the lender must obtain a certificate of completion from a qualified appraiser before it delivers the mortgage to us. The certification does not need to include photographs of the property, unless those photographs that accompanied the original appraisal report are no longer representative of the completed property.

Generally, the original appraiser should complete any required certification of completion; however, the lender may use a substitute appraiser. In such cases, the substitute appraiser must review the original appraisal and certify that the original appraiser’s description of the property was accurate that the opinion of market value was reasonable on the date of the original appraisal report. The lender should note in its files why the original appraiser was not used.