

Selling Guide Announcement SEL-2014-14

November 20, 2014

Lender Selling Representations and Warranties Framework Updates

With this Announcement, Fannie Mae, jointly with Freddie Mac and at the direction of the Federal Housing Finance Agency (FHFA), is announcing a number of significant enhancements to the selling representations and warranties framework introduced in Announcement SEL-2012-08, *New Lender Selling Representations and Warranties Framework* (version 1 of the framework), and updated earlier this year in Announcement SEL-2014-05, *Lender Selling Representations and Warranties Framework Updates* (version 2 of the framework). These changes relate to the framework's life of loan representations and warranties for misstatements, misrepresentations, omissions, and data inaccuracies.

In addition to the changes to the framework, Fannie Mae is also updating the section of the *Selling Guide* related to compliance with laws in order to provide lenders with more certainty and transparency regarding when and how Fannie Mae will be able to enforce remedies for compliance with laws violations.

Effective Dates

The changes to the framework are effective retroactively for whole loans purchased, and mortgage loans delivered into MBS with pool issue dates, on and after January 1, 2013, except that these changes do not apply to any loans for which Fannie Mae has issued a repurchase request prior to November 20, 2014. The changes to the *Selling Guide* provisions regarding compliance with laws are effective for whole loans purchased on and after November 20, 2014, and for mortgage loans delivered into MBS with pool issue dates on and after December 1, 2014.

It is Fannie Mae's expectation that any future modifications to the framework will apply prospectively.

Background

Under the framework, lenders are relieved of certain selling representations and warranties set forth in Subparts B1–B5 of the *Selling Guide* that relate to the underwriting of the borrower, the property, or the project for loans delivered to Fannie Mae that have achieved an acceptable payment history or a successful full-file quality control review by Fannie Mae. Under the framework, lenders are not relieved from Fannie Mae's enforcement of its representations and warranties with respect to the following matters ("life of loan representations and warranties"), even if the issues are referenced in Subparts B1–B5 of the *Selling Guide*:

- Charter Matters;
- Misstatements, Misrepresentations, and Omissions;
- Data Inaccuracies;
- Clear Title/First-Lien Enforceability;
- Compliance with Laws and Responsible Lending Practices; and
- Single-Family Mortgage Product Eligibility.

The representations and warranties in the *Selling Guide* that do not relate to the underwriting of the borrower, the property, or the project (for example, MBS pool delivery representations and warranties) are not eligible for relief under the framework.

Fannie Mae is updating the *Selling Guide* to provide lenders with more certainty regarding when Fannie Mae will enforce remedies, including repurchase, related to the life of loan exclusions for misstatements, misrepresentations, omissions and data inaccuracies. Lenders will only be required to repurchase loans with misrepresentations or data inaccuracies if the misrepresentations or data inaccuracies are significant, as defined below, and the loan was not eligible for sale to Fannie Mae.

This Announcement also includes information related to post-relief mortgage file reviews and reminders related to a lender's rights to cure a defect and to appeal a repurchase request as part of the repurchase rebuttal process, as described in the *Selling Guide*.

Changes to the Life of Loan Representations and Warranties

Misstatements, Misrepresentations, and Omissions

For loans that have obtained relief under the framework, Fannie Mae is updating the life of loan exclusion for misstatements, misrepresentations, and omissions, as specified below.

"Misrepresentations" means any misstatements, misrepresentations, or omissions by any party to the loan transaction pertaining to the borrower, the property, or the project, that are made with or without the lender's knowledge, and that

1. involve three or more loans delivered to Fannie Mae by the same lender;
2. were made pursuant to a common pattern of activity in connection with loan origination or sale, based on information in the loan file or other facts or circumstances that existed at the time of delivery of the loan to Fannie Mae that involve at least one party common to all of the loans;
 - (a) if the selling lender is the common party, involve the same individual; or
 - (b) if a third party is the common party, involve the same individual or entity;and
3. are "significant" in that using true and accurate information, either
 - (a) Fannie Mae determines that the loan would not have been eligible for sale to Fannie Mae under the terms of the lender's contract with Fannie Mae in effect at the time of delivery of the loan; or
 - (b) Fannie Mae determines that the loan would have been eligible for purchase, but under different terms.

For purposes of finding three or more loans to constitute the pattern, both loans that have obtained relief under the framework and loans that have not obtained relief may be counted. If loans that have not obtained relief are counted for purposes of establishing the pattern, those loans must meet all requirements of this exclusion (three or more loans, common pattern of activity, significance) in order for Fannie Mae to enforce a remedy for each loan.

In determining whether a misrepresentation is significant, Fannie Mae will rely on its Desktop Underwriter[®] (DU[®]) simulator. The DU simulator will use the true and accurate loan information to approximate the DU recommendation as of the time of delivery and compare it to the DU recommendation the lender obtained in the final DU loan submission before delivery. If the loan originally did not have a DU recommendation, the DU simulator will compare the new DU recommendation to the DU recommendation the loan would have received using the data provided at delivery, had the lender used DU.

A misrepresentation will be considered significant and the lender will be required to repurchase the loan only if the loan receives a worse DU recommendation from the simulator than it received (or would have received) at

the time of delivery to Fannie Mae, except that Fannie Mae will also take into account any applicable variance and the impact of any undisclosed concessions, concealed transaction terms, or other violations of the lender's contract (including *Selling Guide* requirements) that are involved in the misrepresentation, but are not evaluated by the DU simulator, when determining significance. Fannie Mae will notify the lender of any such undisclosed matters or violations that are considered in connection with determining significance. Fannie Mae will provide the lender with documentation supporting the significance determination.

If Fannie Mae determines that the loan would have been eligible for sale but under different terms than those under which the loan was sold, as described in 3(b) above, Fannie Mae will not seek repurchase, but instead will re-price the loan, consistent with the lender's contract at the time of delivery, to reflect the true risk profile of the loan.

As an exception to the above, a loan involving fraud will be subject to repurchase regardless of whether the above test (three or more loans, common pattern of activity, significance) has been met. For purposes of this life of loan exclusion only, "fraud" is established either by

- an adjudicated claim affirming fraud by or against the lender or other party to the loan transaction; or
- Fannie Mae finding clear and convincing evidence that a lender or other party to the loan transaction knowingly executed or participated in a scheme or artifice in connection with the underwriting, origination, or sale of a loan
 - to defraud Fannie Mae or any other party to the loan transaction; or
 - to obtain any moneys, funds, credits, assets, securities, or other properties from Fannie Mae or any other party to the loan transaction by means of fraudulent pretenses, representations, or promises.

Data Inaccuracies

For loans that have obtained relief under the framework, Fannie Mae is updating the life of loan exclusion for data inaccuracies as specified below.

"Data inaccuracies" are delivery data (Uniform Loan Delivery Dataset (ULDD)) inaccuracies pertaining to the underwriting of the borrower, the property, or the project, if and to the extent

1. the data inaccuracies affect five or more loans and involve the same delivery data element(s);
2. the ULDD data differs from information in the lender's mortgage loan files; and
3. the data inaccuracies are "significant" in that using the information from the loan file to qualify the borrower, property, and/or project, either
 - (a) Fannie Mae determines that the loan would not have been eligible for sale under the terms of the lender's contract with Fannie Mae in effect at the time of delivery of the loan, or
 - (b) Fannie Mae determines that the loan would have been eligible for sale to Fannie Mae, but under different terms.

For purposes of finding five or more loans involving the same data element inaccuracy, both loans that have obtained relief under the framework and loans that have not obtained relief may be counted. If loans that have not obtained relief are counted for purposes of establishing that there were five or more loans with the same data element inaccuracy, those loans must meet all other requirements of this exclusion (same delivery data elements, data differs from information in the loan file, significance) in order for Fannie Mae to enforce a remedy for each loan.

In determining whether the data inaccuracies are significant, Fannie Mae will rely on the DU simulator. The DU simulator will use the true and accurate loan information to approximate the DU recommendation as of the

time of delivery and compare it to the DU recommendation the lender obtained in the final DU loan submission before delivery. If the loan originally did not have a DU recommendation, the DU simulator will compare the new DU recommendation to the DU recommendation the loan would have received using the data provided at delivery, had the lender used DU.

A data inaccuracy will be considered significant and the lender will be required to repurchase the loan only if the loan receives a worse DU recommendation from the simulator than it received (or would have received) at the time of delivery to Fannie Mae, except that Fannie Mae will also take into account any applicable variance entered into with the lender when determining significance. Fannie Mae will provide the lender with documentation supporting the significance determination.

If Fannie Mae determines that the loan would have been eligible for sale using the accurate information from the loan file, but under different terms than those under which the loan was sold, as described in 3(b) above, then Fannie Mae will not seek repurchase but instead will re-price the loan, consistent with the lender's contract at the time of delivery, to reflect the true risk profile of the loan.

Single-Family Mortgage Product Eligibility/Unacceptable Mortgage Products

The Single-Family Mortgage Product Eligibility life of loan exclusion will now be called Unacceptable Mortgage Products. Although the lender must reference the *Selling Guide* in order to determine whether a loan is acceptable for sale to Fannie Mae, Fannie Mae will list examples of unacceptable mortgage products in this life of loan exclusion to the framework. The non-exhaustive Single-Family Mortgage Product Eligibility list in A2-2.1-06, Life of Loan Representations and Warranties, will be updated accordingly. Fannie Mae will not expand this list by adding features related to the underwriting of the borrower, the property, or the project.

Post-Relief Loan File and Appraisal Reviews

Fannie Mae may perform loan file reviews for quality assurance and audit purposes both before and after a loan obtains relief under the framework. However, Fannie Mae cannot issue a repurchase request or seek an alternative remedy with respect to a deficiency in the underwriting of the borrower, the property, or the project that is relieved under the framework (such as a deficiency related to the LTV ratio or debt-to-income ratio) that is discovered after the loan has obtained relief, except to the extent the deficiency involves one of the life of loan exclusions or another provision of the *Selling Guide* that is not relieved under the framework. If, after a loan has obtained relief under the framework, Fannie Mae reviews an appraisal and determines that the property value used to calculate the LTV ratio was incorrect at the time of delivery, Fannie Mae will not issue a repurchase request based solely on the fact that the newly calculated LTV ratio is over 80% and the loan did not have credit enhancement in place when it was delivered to Fannie Mae.

Reminders Relating to Lenders' Right to Cure and to Appeal Repurchase Requests

As a reminder, a lender may cure underwriting and origination defects that are capable of being cured consistent with the *Selling Guide*. After a lender has cured a loan defect in the time and manner specified in the *Selling Guide*, Fannie Mae cannot enforce a remedy based on the breach of the cured defect.

Also, as a reminder, lenders may appeal repurchase requests issued for breaches of life of loan representations and warranties as part of the repurchase rebuttal process.

Other Changes to the *Selling Guide*

Compliance with Laws

In addition to the above changes to the framework, Fannie Mae is also updating the *Selling Guide*, A3-2-01, Compliance with Laws, which among other things requires lenders to comply with applicable federal, state and

local laws. These changes are effective for whole loans purchased on and after November 20, 2014, and for mortgage loans delivered into MBS with pool issue dates on and after December 1, 2014, without regard to whether the loan has obtained relief under the framework.

Under the current *Selling Guide* provision, Fannie Mae may enforce a remedy for all lender violations of applicable federal, state and local laws that may have a material effect on Fannie Mae. To provide more transparency and certainty to lenders, Fannie Mae is limiting those situations for which it may enforce a repurchase to those situations in which:

1. the lender's failure to comply could be expected to impair Fannie Mae's or its servicer's ability to enforce the note or mortgage;
2. the lender's failure to comply could be expected to impose assignee liability on Fannie Mae; or
3. the loan is found to have been in violation of, or if Fannie Mae has made a finding, based on the facts available to Fannie Mae, that a violation may have occurred, of one or more of the following laws or related regulations:
 - Office of Foreign Assets Control (OFAC) of the Department of Treasury laws and regulations;
 - Fair Housing Act;
 - Anti-discrimination provisions of the Equal Credit Opportunity Act (ECOA);
 - Unfair, Deceptive or Abusive Acts or Practices under federal and state law (UDAAP); or
 - Securities Exchange Act of 1934.

With respect to UDAAP, Fannie Mae will take into consideration published federal and state announcements of interpretations as well as all published judicial and administrative decisions and will not enforce a repurchase if the matter can be cured by remediation to the injured party and the lender makes such remediation. However, three or more years after the acquisition (or MBS pool issue date) of a loan, Fannie Mae may not seek repurchase on UDAAP grounds regarding a specific practice unless a lender self-reports or a federal or state enforcement authority has indicated, asserted, or claimed that such practice violates or may violate UDAAP, or a federal or state court has held that a specific practice violates UDAAP.

A repurchase request based on a compliance with law violation will include supporting facts and findings made by Fannie Mae in the course of considering the facts and circumstances before it. Fannie Mae's determination that a violation has occurred must be consistent with the facts and circumstances provided by the lender and any other information obtained by Fannie Mae as part of its evaluation of the situation.

If Fannie Mae issues a repurchase request in connection with a failure to comply with laws when there is pending litigation underway involving that same issue or a government agency with authority to make a determination regarding the issue has publicly stated that it is reviewing the issue, the lender will not be required to repurchase the loan until 30 days after the litigation has been dismissed, settled, or concluded at trial in an adjudication or the government agency has made a final determination (collectively, the "Resolution"). After the Resolution, the lender may request that Fannie Mae review the appropriateness of the repurchase request in light of the Resolution, and Fannie Mae will withdraw the repurchase request where appropriate.

The lender is obligated to indemnify Fannie Mae for losses, judgments, damages, claims, costs, expenses, legal actions, and legal fees related to any claim of non-compliance with laws.

As previously announced, Fannie Mae will not issue a repurchase request based on violations of the ability to repay provisions under the Truth in Lending Act (ATR) unless a court or regulator concludes the loan did not comply with ATR.

Responsible Lending Practices

The provisions in the *Selling Guide* that address responsible lending practices also reflect other underwriting practices that may overlap with the substance of representations and warranties covered in Subparts B1–B5 of the *Selling Guide* that are subject to relief. In the interest of clarity, Fannie Mae is revising A3-2-02, Responsible Lending Practices, to reflect that the portion of A3-2-02 entitled “Underwriting Standards” is relieved under the representation and warranty framework (subject to applicable life of loan exclusions). However, the framework does not grant lenders relief from the first part of A3-2-02 relating to Fannie Mae’s responsible lending practices.

Future Guide Updates

These policy changes will be included in a future update of the *Selling Guide*.

Lenders who have questions about this Announcement should contact their Account Team.

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