



**DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**

WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-  
FEDERAL HOUSING COMMISSIONER

**Date: December 16, 2009**

**To: All Approved Mortgagees**

**Mortgagee Letter 09-52**

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**Subject** Short Sales and Short Pay Offs

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**Purpose** This mortgagee letter provides guidance to lenders and underwriters regarding borrower eligibility when

- a previously owned property was sold for less than what was owed (short sale), or
- there is principal write down of indebtedness that cannot be refinanced into a new mortgage (short pay off).

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**Effective Date** This guidance is effective immediately.

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**Affected Topics** The topics summarized below were revised or created as a result of these changes in guidance. This Mortgagee Letter also provides the entire content of each block affected, with changes underlined. The changes will be integrated into the FHA Single Family On-Line Handbooks shortly.

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### **Mortgagee Letter 09-52, Continued**

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#### **Summary – FHA Guidance on Short Sales**

Borrowers are not eligible for a new FHA mortgage if they pursued a short sale agreement on his or her principal residence simply to

- take advantage of declining market conditions, and
- purchase, at a reduced price, a similar or superior property within a reasonable commuting distance.

**Reference:** For detailed information on converting existing principal residences into rental properties, see 4155.1 4.E.4.g

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#### **Summary – Guidance on Borrowers current at the time of Short Sale**

Borrowers are considered eligible for a new FHA-insured mortgage if

- they were current on their mortgage and other installment debts at the time of the short sale of their previously owned property, and
- the proceeds from the short sale serve as payment in full.

**Reference:** For detailed information, see “*Short Sales*” at 4155.1 4.C.2.1.

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#### **Summary – Guidance on Borrowers in default at the time of Short Sale**

Borrowers in default on their mortgage at the time of the short sale (or pre-foreclosure sale) are not eligible for a new FHA-insured mortgage for three years from the date of the pre-foreclosure sale. Lenders may make exceptions to this rule under certain circumstances.

**Reference:** For detailed information, see “*Short Sales*”, at 4155.1 4.C.2.1.

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**Mortgagee Letter 09-52, Continued**

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**Summary –  
Refinancing  
with Short Pay  
Off**

FHA will insure the first mortgage where the existing note holder(s) write off the amount of indebtedness that cannot be refinanced into the new mortgage due to a decline in property value and/or a reduction in income.

**Reference:** For detailed information, see “*Short Pay Offs*”, at 4155.1 3.B.1.f.

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**Questions**

Please address any questions about the topics addressed in this Mortgagee Letter to the FHA Call Center at 1-800-CALLFHA.

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**Signature**

David H. Stevens  
Assistant Secretary for Housing-Federal Housing Commissioner

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# Mortgagee Letter 09-52, 4155.1 Chapter 4.C.2. New Topic (changes underlined)

## I. Short Sales

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### 4155.1 4.C.2.1 Short Sales

Borrowers are not eligible for a new FHA- insured mortgage if they pursued a short sale agreement on his or her principal residence simply to

- take advantage of declining market conditions, and
- purchase at a reduced price a similar or superior property within a reasonable commuting distance.

*Reference:* For detailed information on converting existing principal residences into rental properties, see 4155.1 4.E.4.g

#### **Borrowers Current at the time of Short Sale**

Borrowers are considered eligible for a new FHA-insured mortgage if, from the date of loan application for the new mortgage

- All mortgage payments due on the prior mortgage were made within the month due for the 12 month period preceding the short sale, and
- All installment debt payments for the same time period were also made within the month due.

#### **Borrowers in Default at the time of Short Sale**

Borrowers in default on their mortgage at the time of the short sale (or pre-foreclosure sale) are not eligible for a new FHA-insured mortgage for three years from the date of the pre-foreclosure sale.

*Note:* Borrowers who sold their property under FHA's pre-foreclosure sale program are not eligible for a new FHA-insured mortgage from the date that FHA paid the claim associated with the pre-foreclosure sale.

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### **Mortgagee Letter 09-52, 4155.1, Chapter 4.C.2. New Topic (changes underlined)**

#### **I. Short Sales, Continued**

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**Short Sales**  
(continued)

**Exceptions:** Lenders may make exceptions to this rule for borrowers in default on their mortgage at the time of the short sale if

- The default was due to circumstances beyond the borrower's control (such as death of primary wage earner, long term un-insured illness, etc.), and
- The review of the credit report indicates satisfactory credit prior to the circumstances beyond the borrower's control that caused the default.

**Reference:** For information on *Short Pay Offs*, see 4155.1 3.B.1.f.

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### **Mortgagee Letter 09-52, 4155.1, Chapter 3.B.1. New Topic (changes underlined)**

#### **f. Short Pay Offs**

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**4155.1 3.B.1.f.**  
**Short Pay Offs**

To be eligible for refinancing with a short pay off, borrowers must be current on their mortgage.

**Reference:** For more information on mortgage payment history, see 4155.1 4.C.2.b.

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### **Mortgagee Letter 09-52, 4155.1, Chapter 3.B.1. New Topic (Changes underlined)**

#### **f. Short Pay Offs, Continued**

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##### **Short Pay Offs (continued)**

FHA will insure the first mortgage where the existing note holder(s) write off the amount of the indebtedness that cannot be refinanced into the new FHA-insured mortgage if

- there is insufficient equity in the home based on its current appraised value, and/or
- the borrower has experienced a reduction in income and does not have the capacity to repay the existing indebtedness against the property.

For instances where the existing note holders are reluctant to write down indebtedness, a new subordinate lien may be executed by the amount which the payoff is short. For more information on new subordinate financing see 4155.1 3.B.1.c.

If payments on subordinate financing are required, they must be included in the qualifying ratios unless payments have been deferred for no less than 36 months. This policy only applies to no cash-out (rate and term) refinances with short pay offs.

***Reference:*** For information on *Short Sales*, see 4155.1 4.C.2.1.

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