



## “HOPE FOR HOMEOWNERS” Refinance Program Announced by HUD

On October 1, 2008, the Bush Administration announced implementation of a Department of Housing and Urban Development (HUD) and Federal Housing Administration (FHA) refinance program to help troubled homeowners. The program entitled, “*Hope for Homeowners*” (HOPE Program), will offer homeowners having difficulty making mortgage payments, an opportunity to refinance first mortgages at a reduced principal balance. Loans refinanced under the program will be insured by the FHA.

Signed into Law by President Bush in July of 2008<sup>1</sup>, a new § 1715z-23 was added to *Title 12. Bank and Banking, Chapter 13. National Housing Mortgage Insurance*. The program, which is voluntary for lenders, commits \$300 billion and provides for government guarantees of the mortgages refinanced under it. The current maximum loan amount available to a homeowner under the HOPE program is \$554,440.00, which would seem to cover a broad range of home values. The program will continue until September 30, 2011.

The program offers a fixed rate mortgage for owner occupied one-to-four family residences (HOPE Mortgage). *The program applies only to existing first mortgages originated after January 1, 2008.* Borrowers must establish an inability to make mortgage payments and “*a ratio of mortgage debt to income, taking into consideration all existing mortgages of that mortgagor at such time, greater than 31 percent (or such higher amount as the Board determines appropriate).*” As an additional requirement, the borrower must not own an interest in any other residence. Homeowners meeting these criteria may be eligible to have their mortgage refinanced at up to 90% (or

higher as determined by the HOPE Board) of the current appraised value of the property.

Participation in the program requires that the existing first mortgage lender, and any subordinate mortgagees, accept the proceeds of the HOPE Mortgage as consideration for a discharge of their lien and waive prepayment and late payment fees. Subordinate mortgage lenders will receive a certificate evidencing their interest as an obligation backed by HUD with payment conditioned on the value of HUD’s appreciated share in the property. Borrowers are prohibited from making subordinate mortgages for the first five years of the term of the HOPE Mortgage, except, if necessary, for the maintenance or preservation of the property.

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As an additional requirement, the HOPE Mortgage will allow the Department of Housing and Urban Development (HUD) to share in any equity or appreciation in the value of the property securing the HOPE Mortgage. The HUD interest is in the equity created by the HOPE Mortgage and in any appreciation in the value of the property is secured by the

borrower executing a *Shared Equity Note, Shared Appreciation Note, Shared Equity Mortgage (collectively the “SEM” documents) and Shared Appreciation Mortgage (the “SAM” mortgage).* The SEM and SAM mortgage interests are secured by second and third priority mortgage liens, respectively, against the property.

SEM documents secure the recapture of the Equity created by the HOPE Mortgage upon a refinancing of the HOPE Mortgage or disposition of the property other, than arms length sale for more than the HOPE Mortgage amount (*being the difference between the value of the property and the HOPE Mortgage at origination*). The SEM also secures the appreciation in value arising from an arms length sale (*being the difference between appraised value at date of sale and the HOPE Mortgage at origination*).

<sup>1</sup> Title IV, § 1402(a), 122 Stat. 2800; Oct. 3, 2008, P.L. 110-343, Div A)

The "Shared Equity" interest of HUD is phased-in during the first five years from the origination of the HOPE Mortgage, on a sliding percentage scale starting at 100% of equity, decreasing by 10% each year thereafter, to a floor of 50%. The "Shared Appreciation" feature is fixed at a flat 50% of the appreciated value of the property. HUD uses the Shared Equity to repay the prior first mortgage lender and any subordinate mortgagee. The Shared Appreciation is used to repay subordinate lenders who, like the first mortgage lender, were required to release liens for less than full payment, and in the case of subordinate mortgagees, possibly no payment of their outstanding indebtedness. Any overage collected by HUD goes to the FHA.

In its October announcement HUD described the Shared Equity program as follows.

*If the home is sold or refinanced, the homeowner will share the equity with FHA on a sliding scale ranging from a 100 percent FHA share after the first year to a minimum of 50 percent after five years. The lien holder that previously held the highest priority will receive payment up to a proportion of its original interest, not to exceed the amount of available appreciation. This type of delayed payoff will take place until all prior lien holders are satisfied or the amount of available appreciation is exhausted. All remaining appreciation is remitted to FHA.*

Additional requirements and features of the program are payment of a mortgage insurance premium of 3% and an annual premium of 1.5%. Closing costs may be financed in the HOPE Mortgage, not to exceed 90% of appraised value, including the mortgage insurance premium. Closing costs may also be paid directly by the borrower or by the servicing lender or a third party, i.e., under any federal, state or local assistance program.

In New York, the SEM and SAM would be exempt from mortgage taxes as the mortgagee is the Department of Housing and Urban Development. It should be noted that the shared appreciation feature is presently found in Reverse Mortgages, authorized under NY Real Property Law §§ 280, 280-a and Tax Law § 252-a. Will the Shared Equity and Shared Appreciation features of the HOPE Mortgage program raise "equity clogging" issues in NY remains to be seen, however, such state issues may be preempted by the provisions of 12 U.S.C. § 1735f-7a.

The success of the program is dependant on lender willingness to surrender its priority lien position for a partial payment or, in the case of subordinate mortgage lenders, only a promise of some payment in the future. The program only applies to loans originated after January 1, 2008 when rates had started to fall, and lenders under scrutiny and under predatory lending laws began to back away from "liar loans" and loans with "teaser rates." It is probably fair to say that this program targets borrowers not only having difficulty making payments, but who have also suffered from the real estate crash which makes refinancing or selling difficult or impossible.

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## FINAL REGULATIONS ISSUED, SOVEREIGN WEALTH FUND INVESTMENTS IN U.S. REAL PROPERTY SUBJECT U.S. GOVERNMENT REVIEW.

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**A** Sovereign Wealth Fund (SWF) is the investment vehicle of foreign governments having surplus funds from various sources, i.e., central bank reserves or derived from tax revenues, budget surpluses or surplus revenue from export sales of state owned natural resources. Governments with excess cash will, not unlike holders of private capital, seek to invest their funds by buying foreign revenue producing assets.

Early this year, Southeast Asian and Middle East governments provided \$21 billion to two major U.S. banking institutions that had suffered significant losses from the ongoing credit crisis.<sup>1</sup> Previously, in a much debated 2006 transaction, a moderate Middle East government's SWF attempted to purchase the foreign operator of six major U.S. port facilities.<sup>2</sup> As a result of growing U.S. security concerns and fears of instability in the Middle East, the deal raised significant furor in this Country despite it being backed by the Bush Administration. As a result Congress passed the *Foreign Investment and National Security Act of 2007 (FINSA)*.<sup>3</sup>

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<sup>1</sup> Citigroup and Merrill Lynch.

<sup>2</sup> In February 2006 the Peninsular and Oriental Steam Navigation Company (P&O), a British shipping company proposed to sell its port management operations to DP World, a government owned entity of Dubai in the United Arab Emirates.

<sup>3</sup> 50 USC Appx § 2170.

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For the purposes of FINSA, § 800.216 defines a Foreign person as

- (a) Any foreign national, foreign government, or foreign entity; or
- (b) Any entity over which control is exercised or exercisable by a foreign national, foreign government, or foreign entity.

This past November, final rules were published in the Federal Register clarifying what transactions are deemed covered under FINSA.<sup>4</sup> The rules set-out in Sub-Part C provide the following:

Transactions are covered transactions include, without limitations: (§ 800.301)

- a. A transaction which, irrespective of the actual arrangements for control provided for in the terms of the transaction, results or could result in control of a U.S. business by a foreign person.
- b. A transaction in which a foreign person conveys its control of a U.S. business to another foreign person.
- c. A transaction that results or could result in control by a foreign person of any part of an entity of assets, if such part of an entity or assets constitutes a U.S. business. (See § 800.302(c))

Transactions that are not covered transactions include without limitation: (§ 800.302)

- a. A stock split or pro rata stock dividend that does not involve a change in control.
- b. A transaction that results in a foreign person holding ten percent or less of the outstanding voting interest in a U.S. business (regardless of the dollar value of the interest so acquired), but only if the transaction is solely for the purpose of passive investment. (See § 800.223)
- c. An acquisition of any part of an entity or of assets, if such part of an entity or assets do not constitute a U.S. business. (See § 800.223)
- d. An acquisition of securities by a person acting as a securities underwriter, in the ordinary course of business and in the process of underwriting.

- e. An acquisition pursuant to a condition in a contract of insurance relating to fidelity, surety, or casualty obligations if the contract was made by an insurer in the ordinary course of business.

The examples provided in the regulations under § 800.301(c), Example 7, include as a covered transaction the purchase of an operating business *together with its real estate assets*. However, Example 6 of that section instructs that the purchase of only real property (and improvements) without any business operations associated with it would not be a covered transaction.

Pursuant to § 2170(b)(2)(D), an otherwise covered transaction may not be subject to review if the Secretary of the Treasury and the head of the lead agency jointly determines, on the basis of review "*that the transaction will not impair the national security of the United States.*" While it is probable that the transaction would be allowed, review of the "*covered transaction*" is required.

The Committee on Foreign Investment in the United States was established under Executive Order No. 11858. The members are the Cabinet Secretaries of the major Cabinet Departments, i.e., Treasury, Homeland Security, Commerce, Defense, State, Attorney General, Energy, Labor (a nonvoting, ex-officio member) and also, the Director of National Intelligence (also a nonvoting, ex-officio), as well as heads of any other executive department, agency, or office, as the President determines would be appropriate, on a case-by-case basis.

The Secretary of the Treasury is the chairperson of the Committee. The Law also provides for the appointment of an Assistant Secretary for the Department of the Treasury who reports directly to the Undersecretary of the Treasury for International Affairs and whose duties in respect to the Committee are delegated by the Secretary of the Treasury.

It is obvious that practitioners representing SWF clients, even in less sensitive transactions than the "*DP World*" transaction must be prepared to deal with the Washington bureaucracy, no matter how small the transaction might be.

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<sup>4</sup> 31 CFR Subtitle B, Chapter VIII, Part 800, Sub-Part C, § 800.301 et seq. See also existing Sub-Part B, § 800.201 et seq. (Definitions).

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