
CHAPTER 2 - CHARACTERISTICS OF THE SECRETARY-HELD MORTGAGE (SHM)

- 2-1. GENERAL. HUD's SHM portfolio consists of mortgages that have either been assigned to HUD or are direct loans from HUD (known as purchase money mortgages-PMM). In both cases HUD is the mortgagee.

HUD's rights and responsibilities are limited by the mortgage or deed-of-trust, good business practice, and specific policies and procedures in this handbook and supplements.

Basic mortgage servicing elements covered in this chapter apply to all first mortgages, including SHM's, regardless of any delinquency.

2-2. BASIC DEFINITIONS.

- A. Note: An agreement under which terms a lender will advance money to a borrower for given use and with a specified plan for repayment.
- B. Mortgage: (This term will be used generally throughout the text and includes other variants such as deeds-of-trust) the note security which provides for recovery of the loan proceeds through sale of the property if the borrower defaults.
- C. Lien: A charge on the property, i.e. the right to collect money from the sale of the property.
- 1) Priority: Generally a lien's priority is established by the date and time the lien is legally recorded regardless of which loan was made first.
- 2) Exceptions: Liens for taxes, and in certain States other types of liens (mechanics, etc.), may advance to a first position regardless of their date of record.
- D. Mortgage Servicing is the management and procedures for collecting payments owed by mortgagor to a lender. For Secretary-held mortgages, HUD is the lender.
- 1) Debt Collection. The aim is to collect the debt in an orderly manner so that HUD recovers its investment while the borrower achieves homeownership. Workout of the debt is a viable alternative to foreclosure. Some techniques are discussed in Chapter 4, Servicing the Delinquent Mortgage.

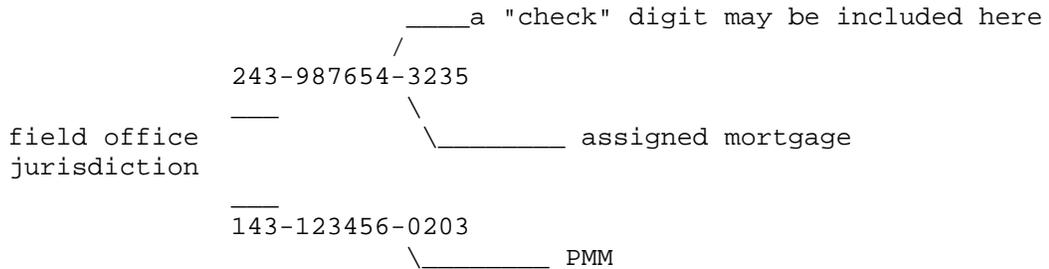
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- 2) Counseling. Counseling can often help the mortgagor reduce

expenses, increase income or improve budgeting. The servicer is not usually expected to act as a counselor; there are agencies that can help the mortgagor search for jobs, find child care, or secure supplementary assistance. Counseling services are discussed in Chapter 4.

- 2-3. TYPES OF MORTGAGES. Mortgages are best categorized by their priority position. Most mortgages in HUD's portfolio are first mortgages securing a loan made to purchase the property. To a lesser extent HUD holds subordinate mortgages that secure other interests--the major class are Section 235 recapture mortgages.

The first nine digits associated with a case are the actual case number and define the office jurisdiction and the numerical sequence of the application for insurance. On recent cases, reading from left to right, a tenth (check) digit has been added for data processing purposes only. The Single Family Mortgage Notes System, discussed later, accommodates this tenth digit but it is not relevant to this discussion.

To differentiate between an assigned mortgage and a PMM, look at the last four (suffix) digits in the FHA case number. If the suffix starts with a "3", it is assigned; if it starts with a "0" it is a PMM. This, fourth from the right digit, is only used on Secretary-Held Mortgages. For example:



- 2-4. MORTGAGE SUBGROUPS. The last three digits in an FHA case number's suffix will indicate the section of the National Housing Act under which they were originally insured and whether the mortgage/note calls for repayment of the loan in equal installments, in variable installments, or if part of the equal installments are subsidized. Example:

262-024680-3221

_____ Mortgage Subgroup

(See Form HUD-428, Home Mortgage APD Code Chart in Exhibit 2-1 for a list of subgroups.)

- A. Equal Installments. Most mortgages in this category bear suffixes such as: 203, 221, etc. They also include mortgages with "buy-down" provisions.
- B. Equal Installments Subject to Subsidy. The suffixes, generally, would be: 235, 256, 265, 256, etc.
- C. Variable Installments. This grouping encompasses a wide variety of loans. They are relatively new in the mortgage market, and complex. Examples are:
 - 1) Graduated Payment Mortgages (GPM). (suffixes 270, etc.) allow the borrower, during the initial years following loan origination, to pay less than that which is necessary to repay the loan in equal installments. The difference is added to the loan balance (negative amortization). However, each year, for a given number of years, the monthly payment increases to compensate for lower initial payments.
 - 2) Growing Equity Mortgages (GEMs). (suffixes 243, 242, etc.) require borrowers to make payments higher than necessary to pay the loan off in equal installments. The additional payments increase annually and are applied to principal and shorten the time to pay off the original loan. The result is that the lender's income (yield) substantially increases. The GEM formalizes, by contract, what any borrower can do by making incremental prepayments to the loan's remaining principal.
 - 3) Adjustable Rate Mortgages (ARMs). (suffixes 229, 529, 729, 230, 530, 730, 231, 531, 731) require that the rate of interest charged on the principal owed under the mortgage be tied to some independent source which, in the case of HUD-insured mortgages, is the weekly average interest rate on United States Treasury Securities adjusted to a constant maturity of one year. This assures that the lender's percentage return on investment is stabilized despite wide variations in its cost of money. Both upward and downward changes are limited and the total number of installments will not change regardless of increases or decreases in the installment payment.

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- 2-5. CHANGING THE MORTGAGE REQUIREMENTS. As noted in Paragraph 2-1 the mortgage establishes rights and responsibilities of the lender and borrower. These specific requirements must be formally amended by mutual agreement if the change adversely affects one of the parties' rights. Such formal changes are often referred to as recasting of the mortgage or replacement (novation) of the mortgage.
 - A. HUD will not recast or replace a mortgage, since doing so can adversely affect the priority of the lien.

