

**DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT****24 CFR Part 203**

[Doc. No. FR-4911-I-01; HUD-2004-0017]

RIN 2502-A118

**Prohibition of Property Flipping in HUD's Single Family Mortgage Insurance Programs; Additional Exceptions to Time Restriction on Sales**

**AGENCY:** Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

**ACTION:** Interim rule.

**SUMMARY:** HUD's regulations addressing the predatory practice of property "flipping" establish certain time restrictions regarding the sale of properties whose purchase is being financed with Federal Housing Administration (FHA) mortgage insurance. The regulations include an exception from the time restrictions for properties acquired and subsequently sold by FHA. This interim rule broadens the exception to include all other federal agencies that acquire properties as a result of a function of their programs and quickly market and sell these acquired properties. The interim rule also clarifies that the time restrictions on sales do not apply to properties that are acquired by inheritance.

**DATES:** *Effective Date:* January 24, 2005.

*Comment Due Date:* February 22, 2005.

**ADDRESSES:** Interested persons are invited to submit comments regarding this rule to the Regulations Division, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410-0500. Electronic comments may be submitted through either:

- The Federal eRulemaking Portal: at <http://www.regulations.gov>; or
- The HUD electronic Web site at: <http://www.epa.gov/feddocket>. Follow the link entitled "View Open HUD Dockets." Commenters should follow the instructions provided on that site to submit comments electronically.

Facsimile (FAX) comments are not acceptable. In all cases, communications must refer to the docket number and title. All comments and communications submitted will be available for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Copies are also available for inspection and

downloading at <http://www.epa.gov/feddocket>.

**FOR FURTHER INFORMATION CONTACT:**

Vance C. Morris, Director, Office of Single Family Program Development, Office of Insured Single Family Housing, Room 9266, Department of Housing and Urban Development, 451 Seventh Street SW., Washington, DC 20410-8000; telephone (202) 708-2121 (this is not a toll free number). Hearing- or speech-impaired individuals may access this number through TTY by calling the toll-free Federal Information Relay Service at (800) 877-8339.

**SUPPLEMENTARY INFORMATION:****I. Background**

On May 1, 2003 (68 FR 23370), HUD published a final rule to address property "flipping," a predatory lending practice whereby a property that was acquired is quickly resold for a considerable profit with an artificially inflated value, often abetted by a mortgagee's collusion with the property appraiser and others involved in the mortgage loan transaction. Most property flipping occurs within a matter of days after the initial acquisition. Minor cosmetic improvements, if any, may be made to the property to make it appeal to an unwary homeowner. The final rule, which became effective on June 2, 2003, restricts flipping by establishing new eligibility requirements for properties whose purchase is being financed with FHA mortgage insurance. These eligibility requirements are contained in a new § 203.37a of HUD's single family mortgage insurance regulations at 24 CFR part 203.

Among other requirements, § 203.37a makes properties that have recently been resold ineligible as security for FHA-insured mortgage financing. Specifically, § 203.37a prohibits FHA insured mortgage financing for any property being sold within three months after acquisition by the seller. Properties that are sold between 91 and 180 days after acquisition by the sellers to homebuyers seeking FHA-insured financing are subject to additional documentation requirements to ensure that any increases in the values of the properties are supportable. The regulation provides that the time restrictions on sales do not apply to sales by HUD of its Real Estate-Owned (REO) properties pursuant to 24 CFR part 291, as well as single family assets in revitalization zones that HUD acquires and sells under the provisions of section 204 of the National Housing Act (12 U.S.C. 1710). The time restrictions are also inapplicable to the

sale of properties acquired by an employer or relocation agency in connection with the relocation of an employee who needs to sell his/her home in order to relocate.

**II. This Interim Rule**

This interim rule broadens the exception to the property flipping time restrictions to include all Federal agencies that acquire properties as a result of a function of their programs and quickly market and sell these acquired properties. This interim rule also clarifies that the time restrictions on sales do not apply to properties that have been acquired by inheritance.

HUD is aware that there are other Federal Government agencies that handle quick sales of acquired single family properties where the purchasers of such properties may want to avail themselves of the ability to obtain FHA-insured mortgage financing. These agencies include, but are not limited to, the Rural Housing Service of the Department of Agriculture, the Department of Veterans Affairs, and the Federal Deposit Insurance Corporation. The Federal Government does not engage in the predatory lending practice of inflating sales prices for the sale of acquired properties under its various programs, and thus, Federal agencies should not be subject to the time restrictions contained in § 203.37a.

In addition to the broadened exception for Federal agencies, this interim rule also clarifies that the time restrictions do not apply to sales of inherited properties. As discussed above, the purpose of the time restrictions is to curb fraudulent property "flips" whereby a property is deliberately acquired through a sale for the purpose of a quick sale at an artificially inflated value. Although an individual who has inherited a property may turn the property over quickly and at a profit, the property was not acquired through a sale. Accordingly, the sales of inherited properties fall outside the intended scope of the regulatory restrictions established by HUD's May 1, 2003, final rule. Since publication of the final rule, HUD has received questions regarding the applicability of the time restrictions on inherited properties. HUD has taken the opportunity afforded by this interim rule to clarify its regulations by specifying that the sale of an inherited property is not subject to the property flipping time restrictions.

HUD has also received questions as to whether the exception could be extended to situations involving bank foreclosures and incidents where a builder has a program to purchase the

old home of an individual buying one of the builder's new homes. HUD understands that lenders and builders have the incentive to turn over these properties quickly. There is more risk, however, that in some of these sales, predatory lending activities could occur. HUD believes that extending the exception to cover these situations would substantially weaken the regulatory safeguards against property flipping. Accordingly, the scope of this interim rule is limited to Federal Government agencies and inherited properties. The broadened exception does not include sales of such properties by the government sponsored enterprises (Fannie Mae and Freddie Mac) nor by private entities.

Although the scope of this interim rule is limited to the two additional exceptions described above (for Federal agencies and inherited properties), HUD recognizes that there may be other circumstances or categories of sales where an exception to the time restrictions may be appropriate and consistent with the goals of the property flipping restrictions. Accordingly, HUD is issuing these regulatory amendments on an interim basis and is providing the public with a 60-day comment period. HUD welcomes comments on the regulatory amendments made by this interim rule and on whether the regulations should provide for additional exceptions to the time restrictions on sales. The public comments will be addressed in the final rule.

### III. Justification for Interim Rulemaking

HUD generally publishes a rule for public comment before issuing a rule for effect, in accordance with its own regulations on rulemaking in 24 CFR part 10. However, part 10 provides for exceptions to the general rule if the agency finds good cause to omit advanced notice and public participation. The good cause requirement is satisfied when prior public procedure is "impractical, unnecessary, or contrary to the public interest" (see 24 CFR 10.1).

This interim rule broadens the exception to the property flipping time restrictions to include all Federal agencies that acquire properties as a result of a function of their programs and quickly market and sell these acquired properties. Since the effective date of HUD's final rule on property flipping, HUD has become aware of instances where individuals wishing to purchase an REO home from another Federal agency have been unable to obtain FHA financing due to the

regulatory time restriction on sales. As noted above in this preamble, the Federal Government does not engage in the predatory lending practice of inflating sales prices for the sale of acquired properties under its various programs. Delaying the effectiveness of this rule to solicit public comment, therefore, would unnecessarily continue to deny FHA mortgage financing to otherwise eligible homebuyers wishing to purchase an REO home from another Federal agency. Accordingly, HUD has determined that it is in the public interest to issue these amendments as an interim rule.

In addition to the broadened exception for Federal agencies, this interim rule also clarifies that the time restrictions do not apply to sales of inherited properties. As explained above in this preamble, transactions involving the sale of inherited properties fall outside the intended scope of the regulatory time restrictions. Since publication of the May 1, 2003, final rule, HUD has received questions regarding the applicability of the time restrictions on inherited properties. HUD has taken the opportunity afforded by this final rule to clarify its regulations by specifying that sales of inherited properties are not subject to the property flipping time restrictions. This amendment does not impose new, nor modify existing, regulatory requirements. Rather, the new regulatory language is designed to clarify the scope of the existing requirements and to assist homebuyers and lenders comply with the HUD requirements. Accordingly, HUD has determined that it is unnecessary to delay the effectiveness of this amendment to solicit prior public comment.

Although HUD believes that good cause exists to publish this rule for effect without prior public comment, HUD recognizes the value of public comment in the development of its regulations. HUD, therefore, is issuing these regulations on an interim basis and is providing the public with a 60-day comment period. HUD welcomes comments on the regulatory amendments made by this interim rule. The public comments will be addressed in the final rule.

### IV. Findings and Certifications

#### *Executive Order 12866, Regulatory Planning and Review*

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866 (entitled "Regulatory Planning and Review"). OMB determined that this rule is a

"significant regulatory action" as defined in section 3(f) of the order (although not an economically significant regulatory action, as provided under section 3(f)(1) of the order). Any changes made to the rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection in the Regulations Division, Room 10276, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410-0500.

#### *Environmental Impact*

A Finding of No Significant Impact with respect to the environment was made for the May 1, 2003, final rule in accordance with HUD regulations at 24 CFR part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332 *et seq.*). That Finding remains applicable to this interim rule and is available for public inspection between the hours of 8 a.m. and 5 p.m. weekdays in the Regulations Division, Room 10276, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410-0500.

#### *Regulatory Flexibility Act*

The Regulatory Flexibility Act (RFA) (5 U.S.C. 601 *et seq.*), generally requires an agency to conduct a regulatory flexibility analysis of any rule subject to notice and comment rulemaking requirements unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. This interim rule does not impose any new or revised obligations of any kind on small entities participating in the FHA single family mortgage insurance programs. Rather, the interim rule is exclusively concerned with alleviating a current burden imposed on Federal agencies that operate REO property disposition programs, and clarifying the scope of current regulatory requirements. Specifically, the interim rule broadens the exception to the property flipping time restrictions to include all Federal agencies that acquire properties as a result of a function of their programs and quickly market and sell these acquired properties. In addition, the interim rule clarifies that the time restrictions do not apply to the sale of inherited properties. To the extent the interim rule has any impact on small entities, it will be to benefit those small entities that assist in the sale of federal REO properties and inherited properties by facilitating the sale of additional properties that otherwise would be

deemed ineligible for FHA insured mortgage financing. Accordingly, the undersigned certifies that this rule will not have a significant economic impact on a substantial number of small entities.

Notwithstanding HUD's determination that this rule will not have a significant economic impact on a substantial number of small entities, HUD specifically invites comments regarding less burdensome alternatives to this rule that will meet HUD's objectives as described in this preamble.

#### *Executive Order 13132, Federalism*

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either imposes substantial direct compliance costs on State and local governments and is not required by statute, or the rule preempts State law, unless the agency meets the consultation and funding requirements of section 6 of the order. This interim rule will not have federalism implications and would not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the order.

#### *Unfunded Mandates Reform Act*

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–

1538) (UMRA) establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments, and on the private sector. This interim rule will not impose any Federal mandates on any State, local, or tribal government, or on the private sector, within the meaning of UMRA.

#### **Catalog of Federal Domestic Assistance**

The Catalog of Federal Domestic Assistance Numbers for 24 CFR part 203 are 14.117 and 14.133.

#### **List of Subjects for 24 CFR Part 203**

Hawaiian Natives, Home improvement, Indians—lands, Loan programs—housing and community development, Mortgage insurance, Reporting and recordkeeping requirements, Solar energy.

■ Accordingly, for the reasons described in the preamble, HUD amends 24 CFR part 203 as follows:

#### **PART 203—SINGLE FAMILY HOUSING MORTGAGE INSURANCE**

■ 1. The authority citation for 24 CFR part 203 continues to read as follows:

**Authority:** 12 U.S.C. 1709, 1710, 1715b, and 1715u; 42 U.S.C. 3535d.

■ 2. Section 203.37a is amended by revising paragraph (c) to read as follows:

#### **§ 203.37a Sale of property.**

\* \* \* \* \*

(c) *Exceptions to the time restrictions on sales.* The time restrictions on sales described in paragraph (b) of this section do not apply to:

(1) Sales by HUD of Real Estate-Owned (REO) properties under 24 CFR part 291 and of single family assets in revitalization areas pursuant to section 204 of the National Housing Act (12 U.S.C. 1710);

(2) Sales by another agency of the United States Government of REO single family properties pursuant to programs operated by these agencies (this does not include the Government Sponsored Enterprises);

(3) Sales of property that were acquired by the sellers by inheritance; and

(4) Sales of properties purchased by an employer or relocation agency in connection with the relocation of an employee.

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Dated: November 22, 2004.

**John C. Weicher,**

*Assistant Secretary for Housing—Federal Housing Commissioner.*

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