

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

[Doc. No. FR-4615-P-01]

RIN 2502-AH57

**Prohibition of Property Flipping in  
HUD's Single Family Mortgage  
Insurance Programs**

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

**ACTION:** Proposed rule.

**SUMMARY:** This proposed rule would address property “flipping,” the practice whereby a property recently acquired is resold for a considerable profit with an artificially inflated value, often abetted by a lender’s collusion with the appraiser. Specifically, the proposed rule would establish certain new requirements regarding the eligibility of properties for FHA mortgage insurance. The proposed regulatory amendments would protect FHA borrowers from becoming unwitting victims of property flipping. Further, the proposed changes comply with Congressional mandates to maintain the FHA Insurance Fund in a sound actuarial manner.

**DATES:** *Comments Due Date:* November 5, 2001.

**ADDRESSES:** Interested persons are invited to submit comments regarding this proposed 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. Communications should refer to the above docket number and title. Facsimile (FAX) comments are not acceptable. A copy of each communication submitted will be available for public inspection and copying between 7:30 a.m. and 5:30 p.m. weekdays at the above address.

**FOR FURTHER INFORMATION CONTACT:** Vance T. Morris, Director, Office of Single Family Program Development, Office of Insured Single Family Housing, Room 9266, U.S. 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 via TTY by calling the toll-free Federal Information Relay Service at (800) 877-8339.

**SUPPLEMENTARY INFORMATION:**

**I. Background**

Predatory lending—whether undertaken by creditors, brokers or even home improvement contractors—involves engaging in deception or fraud, manipulating the borrower through aggressive sales tactics, or taking unfair advantage of a borrower’s lack of understanding about loan terms. These practices are combined with loan terms that, alone or in combination, are abusive or make the borrower more vulnerable to abusive practices. Predatory lending often occurs in the subprime mortgage market which, in general, serves an important role by providing loans to borrowers who do not meet the credit standards for the prime mortgage market.

While no one set of abusive lending practices or terms characterizes a predatory mortgage loan, a loan can be predatory when lenders or brokers undertake one or more of the following practices: Charge borrowers excessive, often hidden fees; successively refinance loans at no benefit to the borrower; make loans without regard to a borrower’s ability to repay; and engage in high-pressure sales tactics or outright fraud and deception. Vulnerable populations, including elderly and low-income individuals, and low-income or minority neighborhoods may be targeted by these unscrupulous lenders.

A major example of predatory lending is property “flipping,” the practice whereby a recently acquired property is resold for a considerable profit with an artificially inflated value, often abetted by a lender’s collusion with the appraiser. Most property flipping occurs within a matter of days after acquisition, and usually with only minor cosmetic improvements, if any.

**II. This Proposed Rule**

This proposed rule is one of several actions HUD is taking to address property flipping. This proposed rule would amend HUD’s FHA single family mortgage insurance regulations at 24 CFR part 203 by establishing a new § 203.37a. This section would prescribe certain new requirements regarding the eligibility of properties for FHA mortgage insurance. The proposed regulatory amendments would protect FHA borrowers from becoming unwitting victims of property flipping. Further, the proposed changes comply with Congressional mandates to maintain the FHA Insurance Fund in a sound actuarial manner. Victims of predatory lending often default, causing losses to the Insurance Fund as a result of claims. Addressing predatory lending

practices will assist in reducing such claims.

1. *Six-month restriction on sales.* Proposed § 203.37a would provide that any property being sold within six months after acquisition by the seller is not eligible for FHA financing. The 6 month restriction would not apply to the disposition of HUD-acquired properties under 24 CFR part 291 or to the disposition of single family assets in revitalization areas pursuant to section 204 of the National Housing Act (12 U.S.C. 1710).

As noted, property flipping involves the rapid resale, often within days, of a recently acquired property. A quick resale minimizes the ownership expenses incurred by the investor, and increases the profitability of the transaction. This is especially true when the “flip” is a pre-arranged transaction that would otherwise not have occurred without an interim owner aware of the final buyer’s willingness to pay the excessive sales price. HUD believes that the proposed 6 month restriction on resales is of sufficient duration to preclude such short-term property flipping. HUD specifically invites public comment on the appropriateness of the 6 month period, and on whether a shorter or longer period would better accomplish HUD’s goal of protecting FHA borrowers from becoming targets of this abusive sales practice.

2. *Owner of record.* Unscrupulous investors will also flip properties they have contracted to purchase (but have not yet acquired) by selling or assigning the rights to the sales contract, often for a significant profit. To prevent such property flipping scenarios, new § 203.37a would provide that only those properties purchased from the owner of record are eligible for FHA mortgage insurance.

3. *Exceptions to property flipping restrictions.* While HUD wishes to assist FHA borrowers in avoiding predatory sales practices, HUD is also aware that justifiable circumstances may sometimes exist for the quick and profitable resale of a recently acquired property. HUD does not wish to prevent the ability to use FHA-insured mortgage financing for the purchase of properties acquired through such legitimate transactions. Accordingly, new § 203.37a would authorize HUD to grant exceptions, on a case-by-case basis, to the proposed property flipping restrictions where the mortgagee demonstrates that the sales price of the property corresponds to its market value. Such documentation may include, but is not limited to, evidence that the sale price reflects a rapidly appreciating real estate market, that the

seller has made improvements that result in a corresponding increase to the value of the property, or that the property is being sold at below market value due to a distress sale or at a tax sale.

HUD invites comment as to whether these exceptions are sufficient to avoid preventing or delaying legitimate business transactions. Such transactions might include certain resales within 6

months at less than the previous purchase price or certain resales at more than the previous purchase price but less than market value.

### III. Findings and Certifications

#### *Public Reporting Burden*

The information collection requirements contained in this proposed rule have been submitted to the Office of Management and Budget (OMB)

under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520). In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

The burden of the information collections in this proposed rule is estimated as follows:

#### REPORTING AND RECORDKEEPING BURDEN

Section reference	Number of parties	Number of responses per respondent	Estimated average time for requirement (in hours)	Estimated Annual Burden (in hours)
§ 203.37a(c) .....	500	1	0.5	250

In accordance with 5 CFR 1320.8(d)(1), HUD is soliciting comments from members of the public and affected agencies concerning this collection of information to:

(1) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;

(2) Evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information;

(3) Enhance the quality, utility, and clarity of the information to be collected; and

(4) Minimize the burden of the collection of information on those who are to respond; including through the use of appropriate automated collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

Interested persons are invited to submit comments regarding the information collection requirements in this proposal. Under the provisions of 5 CFR part 1320, OMB is required to make a decision concerning this collection of information between 30 and 60 days after today's publication date. Therefore, a comment on the information collection requirements is best assured of having its full effect if OMB receives the comment within 30 days of today's publication. This time frame does not affect the deadline for comments to the agency on the proposed rule, however. Comments must refer to the proposal by name and docket number (FR-4615) and must be sent to:

Joseph F. Lackey, Jr., HUD Desk Officer,  
Office of Management and Budget,  
New Executive Office Building,  
Washington, DC 20503;  
and

Ethelene Washington, Reports Liaison Officer, Office of the Assistant Secretary for Housing-Federal Housing Commissioner, Department of Housing and Urban Development, 451 7th Street, SW., Room 9114, Washington, DC 20410

#### *Regulatory Planning and Review*

The Office of Management and Budget (OMB) reviewed this rule under Executive Order 12866, *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 under the Order). Any changes made to this rule as a result of that review are identified in the docket file, which is available for public inspection in the office of the Department's Rules Docket Clerk, Room 10276, 451 Seventh Street, SW, Washington, DC 20410-0500.

#### *Environmental Impact*

A Finding of No Significant Impact with respect to the environment has been made 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. 4223). The Finding of No Significant Impact is available for public inspection between the hours of 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC.

#### *Regulatory Flexibility Act*

The Secretary has reviewed this proposed rule before publication, and by approving it certifies, in accordance with the Regulatory Flexibility Act (5

U.S.C. 605(b)), that this proposed rule would not have a significant economic impact on a substantial number of small entities. The reasons for HUD's determination are as follows. The proposed regulatory amendments are exclusively concerned with curbing the predatory lending practice of property flipping. The vast majority of lenders participating in the FHA single family mortgage insurance programs fully comply with all program requirements and conduct themselves in an ethical manner. The proposed rule would only impact the small minority of unscrupulous lenders who participate in the FHA programs and engage in this predatory practice.

Notwithstanding HUD's determination that this rule will not have a significant economic effect on a substantial number of small entities, HUD specifically invites comments regarding any 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 Executive Order. This proposed rule would 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 Executive Order.

*Unfunded Mandates Reform Act*

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) 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 proposed rule would not impose any Federal mandates on any State, local, or tribal governments, or on the private sector, within the meaning of the Unfunded Mandates Reform Act of 1995.

*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 in 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 proposes to

amend 24 CFR part 203 to read as follows:

**PART 203—SINGLE FAMILY 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. 3535(d).

2. Add § 203.37a to read as follows:

**§ 203.37a Sale of property.**

(a) *Sale by owner of record.* To be eligible for mortgage insurance, the property must be purchased from the owner of record and may not be sold through the sale or assignment of the sales contract.

(b) *No re-sale within previous 6 months.* (1) Any property being sold within six months after acquisition by the seller is not eligible for mortgage insurance.

(2) This six month restriction does not apply to the disposition of:

(i) HUD-acquired properties under 24 CFR part 291; or

(ii) Single family assets in revitalization areas pursuant to section 204 of the National Housing Act (12 U.S.C. 1710).

(c) *Case-by-case exceptions.* HUD may grant exceptions to the provisions of this section, on a case-by-case basis, upon written demonstration by the mortgagee that the sales price of the property accurately corresponds to its market value. Such documentation may include, but is not limited to, evidence that:

(1) The sales price reflects a rapidly appreciating real estate market;

(2) The seller has made improvements that have resulted in a corresponding increase to the value to the property; or

(3) The property is being sold at below market value due to a distress sale or at a tax sale.

Dated: July 12, 2001.

**John C. Weicher,**

*Assistant Secretary for Housing-Federal Housing Commissioner.*

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