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B-162961, Jan. 19, 1968

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B-162961, JAN. 19, 1968

HOUSING - LOANS - DEFAULT - FINANCE CHARGE INCLUSION DECISION TO CERTIFYING OFFICER OF FEDERAL HOUSING ADMIN. CONCERNING CLAIM OF MICHIGAN NATIONAL BANK FOR REIMBURSEMENT OF LOSS ON ACCOUNT OF DEFAULT OF NOTE INSURED BY FHA. IN COMPUTING THE UNPAID BALANCE OF A FHA TITLE I LOAN AT THE TIME A SECOND LOAN IS MADE BY USING THE FHA FORMULA PRESCRIBED IN CASES OF DEFAULT WHICH FORMULA REQUIRES PRORATION OF THE UNPAID BALANCE AND UNEARNED FINANCE CHARGES IS FOR APPLICATION AND, THEREFORE, WHERE INCLUSION OF FINANCE CHARGES AND OUTSTANDING BALANCE MAKE TOTAL EXCEED THE STATUTORY LIMIT OF $3,500 BASED UPON ESTABLISHED FORMULA PAYMENT MAY NOT BE AUTHORIZED. SEE B-137493, 11/20/58.

TO MR. RALPH L. VITALE:

REFERENCE IS MADE TO YOUR LETTER OF NOVEMBER 16, 1967, ASKING WHETHER YOU PROPERLY MAY CERTIFY A VOUCHER ENCLOSED THEREWITH, PAYABLE TO THE MICHIGAN NATIONAL BANK (BANK) IN THE AMOUNT OF $1,622.81. THE VOUCHER COVERS A CLAIM FOR REIMBURSEMENT OF LOSS SUSTAINED ON ACCOUNT OF DEFAULT ON A NOTE THAT HAD BEEN REPORTED FOR INSURANCE BY THE BANK UNDER ITS CONTRACT WITH THE FEDERAL HOUSING ADMINISTRATION (FHA) PURSUANT TO TITLE I OF THE NATIONAL HOUSING ACT, AS AMENDED, 12 U.S.C. 1703. THE DEFAULTED NOTE PROVIDED FOR A NET LOAN TO THE BORROWER IN THE AMOUNT OF $3,000.

IT IS EXPLAINED THAT AT THE TIME THE SECOND LOAN WAS MADE, THE CREDIT APPLICATION SHOWED AN FHA TITLE I LOAN HELD BY ANOTHER LENDER WITH A STATED BALANCE OF $600. AT THE TIME THE CREDIT WAS EXTENDED BY THE BANK ON THE SECOND LOAN REPAYMENTS ON THE EARLIER LOAN WERE CURRENT. SUCH EARLIER LOAN HAD BEEN MADE FOR A TERM OF 60 MONTHS WITH NET PROCEEDS OF $772, PLUS A FINANCE CHARGE OF $190.65, SO THAT THE FACE AMOUNT OF THE NOTE WAS $962.65. AT THE TIME THE BANK EXTENDED CREDIT ON THE SECOND LOAN, TWENTY-THREE PAYMENTS HAD BEEN RECEIVED BY THE OTHER LENDER ON THE PRIOR LOAN. A SUBSEQUENT COMPUTATION OF THE OUTSTANDING BALANCE DUE ON THE PRIOR LOAN AS OF THE DATE OF EXTENSION OF THE SECOND CREDIT, GIVING CONSIDERATION FOR THE UNEARNED FINANCE CHARGE, RESULTED IN THE DETERMINATION THAT AT THE TIME OF EXTENSION OF THE SECOND CREDIT, THERE WAS OUTSTANDING ON THE EARLIER LOAN A BALANCE OF $519.14.

PROVISIONS OF THE NATIONAL HOUSING ACT PERTINENT TO CONSIDERATION OF THE MATTER ARE AS FOLLOWS:

"SECTION 2 (A) (III): * * * THE COMMISSIONER IS AUTHORIZED AND DIRECTED, BY SUCH REGULATIONS OR PROCEDURES AS HE SHALL DEEM ADVISABLE, TO PREVENT THE USE OF ANY FINANCIAL ASSISTANCE UNDER THIS SECTION * * * WHICH WOULD, THROUGH MULTIPLE LOANS, RESULT IN AN OUTSTANDING AGGREGATE LOAN BALANCE WITH RESPECT TO THE SAME

STRUCTURE EXCEEDING THE DOLLAR AMOUNT LIMITATION PRESCRIBED IN THIS SUBSECTION FOR THE TYPE OF LOAN INVOLVED * * *.

"SECTION 2 (B): * * * NO INSURANCE SHALL BE GRANTED UNDER THIS SECTION TO ANY SUCH FINANCIAL INSTITUTION WITH RESPECT TO ANY OBLIGATION REPRESENTING ANY SUCH LOAN, ADVANCE OF CREDIT, OR PURCHASE BY IT (1) IF THE AMOUNT OF SUCH LOAN, ADVANCE OF CREDIT, OR PURCHASE EXCEEDS $3,500: * * *.'

INASMUCH AS THE OUTSTANDING BALANCE ON THE EARLIER LOAN WHEN ADDED TO THE $3,000 ADVANCED BY THE BANK RESULTED IN A TOTAL OF $3,519.14, OR $19.14 IN EXCESS OF THE $3,500 STATUTORY LIMITATION, THE BANK WAS ADVISED BY YOU THAT THE CLAIM COULD NOT BE PAID.

THE BANK, HOWEVER, NOW HAS QUESTIONED WHETHER THE METHOD USED IN COMPUTING THE OUTSTANDING BALANCE ON THE PRIOR LOAN IS REQUIRED BY THE NATIONAL HOUSING ACT.

NEITHER THE NATIONAL HOUSING ACT NOR THE REGULATIONS ISSUED PURSUANT THERETO SPECIFICALLY PRESCRIBE THE MANNER IN WHICH UNPAID BALANCES ARE TO BE DETERMINED. HOWEVER, THE METHOD USED BY FHA TO COMPUTE UNPAID BALANCES IS THE SAME AS THAT SET FORTH IN FHA BOOKLET ENTITLED"TITLE I OPERATING GUIDE" FOR COMPUTING THE UNPAID BALANCE AND EARNED CHARGES ON A DEFAULTED LOAN WHEN A CLAIM IS FILED BY AN INSURED LENDING INSTITUTION. UNDER THAT PROCEDURE, A PRORATION FACTOR REPRESENTS THE RATIO OF THE TOTAL PERIODIC OUTSTANDING BALANCES PRIOR TO THE DATE OF DEFAULT TO THE TOTAL PERIODIC OUTSTANDING BALANCES FOR THE FULL TERM OF THE LOAN. SUCH FACTORS ARE LISTED IN A TABLE OF FACTORS IN A PAMPHLET ENTITLED "TABLES OF PRORATION FACTORS.' BOTH THE BOOKLET AND THE PAMPHLET ARE DISTRIBUTED TO LENDERS AND FINANCIAL INSTITUTIONS HOLDING TITLE I CONTRACTS FOR THEIR USE AND INFORMATION IN PARTICIPATION IN THE TITLE I PROGRAM.

SINCE THERE WAS NO DEFAULT IN THIS CASE, THE AMOUNT OF THE OUTSTANDING BALANCE ON THE FIRST LOAN WAS COMPUTED AS OF THE DATE OF THE SECOND LOAN AND THE METHOD USED WAS THAT DESCRIBED ABOVE. AS PREVIOUSLY STATED THIS RESULTED IN A TOTAL LOAN AMOUNT THAT EXCEEDED THE $3,500 LIMITATION BY $19.14.

THE BANK PAID THE INSURANCE PREMIUM OF $19.30 AS REQUIRED BY SECTION 201.13 (E) OF THE TITLE I REGULATIONS AND SUCH AMOUNT WAS INCLUDED AS A PART OF THE FINANCE CHARGES. THE BANK CONTENDS THAT SINCE UNDER FHA REGULATIONS NO PART OF SUCH PREMIUM CHARGE MAY BE REFUNDED TO THE BORROWER, IT SHOULD NOT BE CONSIDERED AS HAVING BEEN EARNED BY THE BANK AND SHOULD NOT BE INCLUDED IN COMPUTING THE EARNED CHARGE ON THE BASIS THAT IT, IN EFFECT, IS MERELY A TRANSFER FROM THE BORROWER TO THE LENDER AS REIMBURSEMENT FOR THE PREVIOUS PAYMENT BY THE BANK OF THE FHA INSURANCE PREMIUM.

IN A CASE CONSIDERED IN OUR DECISION OF NOVEMBER 20, 1958, B-137493, THE CLAIMANT CONTENDED THAT IT SHOULD BE PERMITTED TO USE A FORMULA BASED ON A CONSTANT RATIO METHOD OF COMPUTING THE YIELD ON THE FINANCING CHARGE. UNDER THAT METHOD THE TOTAL FINANCING CHARGES WOULD BE DIVIDED BY THE NUMBER OF INSTALLMENTS AND THE RESULTING FIGURE WOULD THEN BE USED AS THE PRO RATA AMOUNT OF FINANCING CHARGES TO BE APPLIED WITH EACH PAYMENT. THE USE OF SUCH FORMULA HAD BEEN ACCEPTED THE LOAN THERE INVOLVED WOULD HAVE BEEN UNDER THE STATUTORY LIMITATION.

IN REJECTING THE USE OF SUCH FORMULA WE STATED THAT --

"WHILE THE NATIONAL HOUSING ACT, THE REGULATIONS, AND THE PUBLICATIONS REFERRED

TO ABOVE DO NOT SPECIFICALLY PRESCRIBE THE METHOD TO CALCULATE THE UNPAID BALANCE OF A LOAN FOR DETERMINING THE LIMITATION OF AN ADDITIONAL ADVANCE WE BELIEVE THE REQUIRED USE OF THE METHOD APPLIED BY THE ADMINISTRATION REASONABLY IS TO BE IMPLIED FROM THE PUBLICATIONS. SIMILAR METHODS ARE PRESCRIBED IN THE PUBLICATION PROPERTY IMPROVEMENT LOANS' FOR COMPUTING THE UNEARNED PORTION OF THE FINANCING CHARGES WHEN LOANS ARE REFINANCED, WITH OR WITHOUT ADDITIONAL ADVANCES, AND WHEN REBATES ARE CALCULATED FOR PAYMENTS MADE IN ADVANCE. CERTAINLY NOTHING CONTAINED IN THE PUBLICATION INDICATES OR IMPLIES THAT ANY DIFFERENT METHOD COULD BE USED FOR THE PURPOSE OF CALCULATING THE BALANCE OF A LOAN IN ORDER TO DETERMINE THE MAXIMUM AMOUNT THAT MAY BE ADDITIONALLY ADVANCED WITHIN THE STATUTORY LIMITATION. TO PERMIT THE USE OF THE COMPUTATION CONTENDED FOR BY THE CLAIMANT (WHICH APPARENTLY WAS USED IN CONNECTION WITH ONLY THIS ONE PAYMENT) WOULD HAVE THE EFFECT OF WAIVING COMPLIANCE WITH THE STATUTORY LIMITATION OF $3,500.'

SINCE THE NATIONAL HOUSING ACT DOES NOT PRESCRIBE A FORMULA FOR DETERMINING THE OUTSTANDING BALANCE ON A GIVEN LOAN ON A GIVEN DATE, WE SEE NO BASIS TO DEVIATE FROM THAT PRESCRIBED BY FHA WHICH METHOD CONSISTENTLY HAS BEEN APPLIED BY FHA SINCE THE INCEPTION OF THE TITLE I PROGRAM AND ACCEPTED BY LENDERS IN COMPUTING THE UNPAID BALANCES OF EXISTING LOANS AT THE TIME ADDITIONAL LOANS ARE ADVANCED.

CONCEDING THAT THE METHOD NOW URGED BY THE BANK IS A REASONABLE ONE, NO DOUBT OTHER METHODS COULD BE SUGGESTED THAT ALSO WOULD BE REASONABLE AND PROPERLY COULD BE ADOPTED BY FHA FOR USE IN FUTURE CASES. HOWEVER, UNLESS AND UNTIL A DIFFERENT METHOD IS PRESCRIBED BY FHA THE NEED FOR CONSISTENCY OR UNIFORMITY IN DETERMINING THE UNPAID BALANCES REQUIRES THAT THE METHOD PRESENTLY EMPLOYED BY FHA BE APPLIED IN THE PRESENT CASE.

ACCORDINGLY, AND FOR THE REASONS STATED IN OUR DECISION OF NOVEMBER 20, 1958, REFERRED TO ABOVE, IT IS OUR VIEW THAT SINCE THE TOTAL OF THE LOANS EXCEEDS THE STATUTORY LIMITATION OF $3,500WHEN THE UNPAID BALANCE OF THE FIRST LOAN IS COMPUTED IN THE MANNER CONSISTENTLY REQUIRED BY FHA, THE VOUCHER MAY NOT BE CERTIFIED FOR PAYMENT.