



DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 203

**[Docket No. FR-6029-F-01]
RIN 2502-AJ40**

**Streamlining Warranty Requirements for
Federal Housing Administration (FHA) Single-Family Mortgage Insurance:
Removal of the Ten-Year Protection Plan Requirements**

AGENCY: Office of the Assistant Secretary of Housing – Federal Housing Commissioner, HUD.

ACTION: Final rule.

SUMMARY: This final rule streamlines the home warranty requirements for FHA single-family mortgage insurance by removing the regulations that require borrowers to purchase 10-year protection plans in order to qualify for certain mortgages on newly constructed single-family homes. This action conforms with the changes made by the Housing and Economic Recovery Act of 2008 (HERA). HUD, however, is retaining the requirement that the Warranty of Completion of Construction (form HUD-92544) be executed by the builder and the buyer of a new construction home, as a condition for FHA mortgage insurance. This final rule follows publication of a February 6, 2013, proposed rule, and takes into consideration the public comments received on the proposed rule.

DATES: Effective: **[Insert date 90 days after date of publication in the FEDERAL REGISTER].**

FOR FURTHER INFORMATION, CONTACT: Elissa Saunders, Director, Office of Single Family Program Development, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Room 9184, Washington, DC 20410-8000; telephone number

202-708-2121 (this is not a toll-free number). Persons with hearing or speech impairments may access this number via TTY by calling the Federal Relay Service at 1-800-877-8339.

SUPPLEMENTARY INFORMATION:

I. Background – HUD’s February 6, 2013, Proposed Rule

On February 6, 2013, at 78 FR 8448, HUD published a proposed rule to streamline the inspection and home warranty requirements for FHA single-family home insurance. As part of the February 6, 2013 rule, HUD proposed to eliminate its requirement that borrowers purchase a 10-year protection plan in order to qualify for FHA mortgage insurance for high loan-to-value mortgages where the dwelling was not approved for guaranty, insurance, or a direct loan before the beginning of construction and where the dwelling is less than one year old.¹ In 2008, HERA (Public Law 110-289, 122 Stat. 2654, approved July 30, 2008) eliminated the requirement of purchasing a consumer protection plan or warranty plan for such mortgages. While HUD maintained discretion to keep the requirements in place, HUD is no longer statutorily mandated to do so. Upon evaluation, HUD believes that the significant improvements in building technology and the quality of housing, as well as the adoption of uniform building codes and local jurisdictions’ more stringent enforcement of building codes, mitigate HUD’s previous concerns about needing to protect property owners from defects in workmanship and materials. HUD proposed, however, to retain the requirement that the Warranty of Completion of Construction (form HUD-92544) be executed by the builder and the buyer of a newly constructed home, as a condition for FHA mortgage insurance. This warranty provides assurance to FHA that the home was built according to plan, and protects the buyer against defects in equipment, material, or workmanship supplied or performed by the builder,

¹ Codified at 24 CFR 203.18 and 200-209.

subcontractor, or supplier. The warrantor agrees to fix and pay for the defect and restore any component of the home damaged in fulfilling the terms and conditions of the warranty. The one-year warranty commences on the date that title is conveyed to the buyer, the date that construction is complete, or upon occupancy, whichever date occurs first.

In addition to eliminating the 10-year protection plan requirements and related regulations in 24 CFR 203.18 and 203.200-209, HUD proposed to amend 24 CFR 203.50 to reflect the statutory change made by HERA and the removal of §§ 203.18(a)(3) and 200-209 of the regulations. Section 203.50(f) (“Eligibility of rehabilitation loans”) cross-references § 203.18(a)(3), and because § 203.18(a)(3) was proposed for removal, HUD proposed to also amend § 203.50(f) accordingly.

As part of the same publication, HUD also proposed to eliminate the FHA Inspector Roster (Roster), which is a list of inspectors approved by FHA as eligible to determine if the construction quality of a property is acceptable security for an FHA-insured loan in limited circumstances. HUD had combined the two proposals as they both involved streamlining requirements for FHA single-family mortgage insurance. However, the two proposals are distinct and the regulations unrelated. In addition to covering separate subjects, the regulations applied to different parties. The procedures and requirements related to the Roster applied to inspectors and lenders, while the regulations regarding 10-year protection plans applied to homebuilders, lenders, and borrowers. The public comments reflect this distinction, in that they treated these proposals separately, with the exception of expressions of general support for both proposals. In order to properly address the separate comments received on each proposal and to be more transparent about how the regulatory changes will affect different parties, this final rule

only deals with elimination of the 10-year protection plan requirement. HUD published its final rule removing the FHA Inspector Roster on July 3, 2018 (83 FR 31038).

Interested readers are referred to the preamble of the February 6, 2013, proposed rule for additional historical background and explanation of the proposed regulatory changes.

II. Discussion of the Public Comments Related to the Elimination of the 10-Year Warranty Requirement Received on the February 6, 2013, Proposed Rule

This final rule follows publication of the February 6, 2013, proposed rule, and takes into consideration the public comments received on the proposed rule. The public comment period closed on April 8, 2013. HUD received 7 public comments in response to the proposed rule, 5 of which provided comments on elimination of the 10-year protection plan requirement. These comments were submitted by a fair housing consulting group, a home warranty provider, a housing trade association, a homebuilder, and an individual.²

Three of these comments expressed support for eliminating the 10-year protection plan requirement. Commenters said the requirement for a ten-year warranty is expensive and unnecessarily increases the cost of homeownership to the consumer. One commenter said it agreed with HUD that a 10-year protection plan is no longer necessary to safeguard FHA's insurance fund since the quality of housing, building technology, and building codes and enforcement have improved significantly. This commenter said that the rule would benefit homeowners who choose to purchase a protection plan because there will be additional market competition, as current FHA approved warranty issuers would have to compete with other warranty issuers. Further, the commenter said that eliminating the 10-year protection plan

² The public comments on the proposed rule are available for download from the Regulations.gov website at the following link: <http://www.regulations.gov/#!docketBrowser;rpp=25;po=0;dct=PS;D=HUD-2013-0011>

requirement would relieve warranty providers and HUD of the administrative burdens of application, review, and approval of each warranty plan.

Following is a summary of the significant issues pertaining to the 10-year protection plan requirement raised by the other comments, and HUD's responses. As discussed below, after consideration of all of the comments, HUD has not changed its proposal to eliminate the 10-year protection plan requirement as it was set forth in the February 6, 2013, proposed rule.

Comment: Elimination of the 10-Year Warranty Would Adversely Affect Minority Homeowners. One commenter opposed eliminating the 10-year warranty requirement, writing that African Americans and Hispanic Americans make up a high percentage of FHA mortgage holders, and persons who are eligible for FHA mortgage insurance are those most likely to be targeted with defective products and services and the least likely to have the means to protect their investment if a defect should occur. The commenter wrote that based on the numbers included in the proposed rule used to calculate savings, the average homeowner would pay an annual premium of \$510, which is a significant cost, but a cost that directly benefits the homeowner, unlike other fees designed to protect the investor that have no value to the homeowner.

HUD Response. HUD has not revised the rule in response to this comment. HUD takes its mission to expand affordable homeownership opportunities in a non-discriminatory manner seriously, and believes that the regulatory amendments made by this final rule are consistent with those principles. Although the home warranty has been required, HUD records do not document that a claim has ever been made against the warranty discussed in this rule that resulted in a subsequent claim to FHA for unresolved repairs, damages, or foreclosure. Despite this, as acknowledged by the commenter, the warranty requirements impose a significant cost on FHA

borrowers. Congress recognized these developments and eliminated the statutory requirement for such plans in the FHA programs. This rule follows suit and eliminates the mandate that borrowers purchase such plans. The rule, however, does not prohibit borrowers who desire, and are able to afford, the extra protection from purchasing warranty protection plans. Further, the rule retains the requirement that the Warranty of Completion of Construction (form HUD-92544) be executed by the builder and the buyer of a newly constructed home, as a condition of FHA mortgage insurance.

Comment: Quality of State and Local Codes is Not Sufficiently High to Warrant Removal of 10-Year Warranty Requirement. Two commenters challenged the assertion that the quality of construction standards is sufficiently high enough to warrant the removal of the warranty requirement. The commenters wrote that warranty companies continue to pay out large sums to repair homes due to improper construction, and cited incidents from 2005 to 2008, when thousands of households were exposed to problem drywall, which caused odd odors, corrosion of metal components, failure of electronics and appliances, and physical ailments. A commenter also wrote that because new homes are comprised of thousands of components, and fallible human beings develop the science behind building products, better building and stricter building codes will not prevent construction defects. The commenters wrote that without the 10-year warranty, homeowners face the possibility that the builder may have gone out of business or entered bankruptcy and they are unable to identify the source of the defective materials. The commenters recommended withdrawing this proposed rule and conducting additional research into the number of complaints filed with state regulators and local building code officials.

HUD Response. HUD agrees that the complete elimination of construction defects, while a worthwhile goal is most likely not a feasible outcome given human fallibility and the

limitations of modern technology. HUD does not agree, however, that this justifies the imposition of a costly warranty mandate. The rule does not prohibit homeowners who wish to purchase warranty protection plans from doing so, it only eliminates the mandate that they must purchase such plans. Further, HUD reiterates that the final rule continues to condition FHA mortgage insurance on the Warranty of Completion of Construction (form HUD-92544) which provides assurance that the home was built according to plan and protects the buyer against construction defects. With respect to unforeseen events, such as the concerns noted by the commenter regarding problem drywall, HUD will continue to be at the forefront of efforts to take or support enforcement action, as appropriate, and to provide economic relief for impacted homebuyers. For example, HUD encouraged its mortgage lenders nationwide to consider extending temporary relief to allow families experiencing problems paying their mortgages because of problem drywall, to allow the homeowner time to repair their homes.³ FHA pursued a policy of loan forbearance for one year to borrowers impacted by the drywall problem. Further, the United States Consumer Product Safety Commission (CPSC) and HUD staff representing the Interagency Task Force on Problem Drywall no longer recommended the removal of all electrical wiring in homes with problem drywall after a study conducted on behalf of CPSC was completed. The change in the government's protocol may have reduced the cost of remediation for many homes (CPSC and HUD Issue Updated Remediation Protocol for Homes with Problem Drywall, Release Number 11-176, Release Date: 18, 2011).

III. Findings and Certifications

Regulatory Review - Executive Orders 12866 and 13563

³ See http://portal.hud.gov/hudportal/HUD?src=/press/press_releases_media_advisories/2010/HUDNo.10-068

Under Executive Order 12866 (Regulatory Planning and Review), a determination must be made whether a regulatory action is significant and, therefore, subject to review by the Office of Management and Budget (OMB) in accordance with the requirements of the order. Executive Order 13563 (Improving Regulation and Regulatory Review) directs executive agencies to analyze regulations that are “outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned.” Executive Order 13563 also directs that where relevant, feasible, and consistent with regulatory objectives, and to the extent permitted by law, agencies are to identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public.

This rule was determined to be a “significant regulatory action” as defined in section 3(f) of Executive Order 12866 (although not an economically significant regulatory action, as provided under section 3(f)(1) of the Executive Order). The removal of this requirement is consistent with goals of Executive Order 13563.

The rule does not rise to the level of an economically “significant regulatory action” under section 3(f)(1) of Executive Order 12866. HUD expects the elimination of the 10-year warranty plan to have economic benefits and costs. However, neither the economic costs nor the benefits of the elimination are greater than the \$100 million threshold that determines economic significance under Executive Orders 12866 and 13563. The preamble to the February 6, 2013, proposed rule at 78 FR 8453 -8454, provided a discussion of the anticipated costs and benefits of the regulatory amendments. Please see the below section on the Summary of Benefits and Costs, which summarizes and updates the costs and benefits of the regulatory changes.

[Executive Order 13771](#)

Executive Order 13771, entitled “Reducing Regulation and Controlling Regulatory Costs,” was issued on January 30, 2017. This final rule is considered an EO 13771 deregulatory action. Details on the estimated cost savings of this proposed rule can be found below in the Summary of Benefits and Costs, and in the rule’s Regulatory Impact Analysis.

Summary of Benefits and Costs of Final Rule

Concurrently with this final rule, HUD is publishing its final Regulatory Impact Analysis (RIA) that examines the costs and benefits of this final rule. The RIA is available on-line at: <http://www.regulations.gov>. The major findings in the RIA are presented in this summary.

Reducing risk to borrowers and FHA of substandard construction was the primary purpose of requiring the purchase of a home warranty. Positive trends in the housing sector have weakened the need for such a requirement. Increased quality of construction materials, and the standardization of building codes and building code enforcement, protect consumers better now than when the warranty requirement regulation was first promulgated. Although the home warranty is required, HUD records do not document that a claim has ever been made against the warranty discussed in this rule that resulted in a subsequent claim to FHA for unresolved repairs, damages, or foreclosure. Thus, HUD believes that the benefit in cost savings to consumers would exceed the potential cost of any risk introduced.

To understand the magnitude of the potential gain to consumers, HUD first approximated the resources devoted to the purchase of home warranties. On an annual basis, from 50,000 to 60,000 warranties are issued to FHA borrowers (data provided by FHA). The analysis uses 55,000 to represent a typical year. The average coverage of the mandated warranty plans is \$200,000. The average premium charged under the plans is \$2.70 per \$1,000 of coverage (data provided by warranty companies). The average annual cost per homeowner is approximately

\$540 ($\$2.70/\$1,000 \times \$200,000$). Over ten years, the present value of the \$540 annual payment would range from \$4,060 (at 7 percent) to \$4,740 (at 3 percent).

If the home warranty were a regulatory burden of no utility, then the annual savings to consumers would equal the full amount of the fee of \$540. The aggregate savings would be approximately \$30 million ($\$540 \times 55,000$ warranties). However, the gain is likely less than the estimate of \$30 million. There are homebuyers who would demand and sellers who would supply a long-term warranty even when not required. If a buyer is extremely risk-averse or if a seller prefers to use home warranties to facilitate sales, their purchase of the home warranty would be unaffected by a rule not requiring it. Estimates of the general prevalence of home warranties vary, with studies finding that between 10 and 30 percent of homes have warranties. If 10 percent of homebuyers would have purchased a long-term warranty without the requirement, then consumer savings would be \$27 million, and if 30 percent of homebuyers would have purchased a long-term warranty without the requirement, then the consumer savings would average \$21 million.

The elimination of the warranty requirement also eliminates paperwork burden. Lenders face paperwork burden from reviewing the home warranty before closing. HUD estimates that a lender requires 0.1 hours to process one warranty. Loan officers earn a median hourly wage of \$31;⁴ the opportunity cost of their time would be twice⁵ that, or \$62 per hour. The burden per warranty is \$6.20 (0.1 hours \times \$62). At a volume of 55,000 warranties, the total paperwork burden relieved is \$341,000. Savings will extend to the US government. The elimination of the warranty requirement eliminates the cost to HUD associated with review of the warranty plans submitted for approval and renewal. Administrative burdens to HUD include review of warranty

⁴ <https://www.bls.gov/ooh/business-and-financial/loan-officers.htm>

⁵ Includes benefits, management overhead, rent, employer taxes, and equipment.

plans for acceptance, review of plan renewals, and maintenance of HUD's home warranty webpage.

There is a potential risk to FHA from eliminating the requirement of construction warranties for high-LTV loans. A major structural defect would adversely affect the value of a property and potentially lead to a foreclosure. FHA would bear the cost of the claim directly, and if systemic these costs could be passed on to program participants through higher premiums. Advances in detecting the causes of structural failure reduce both the probability and cost of any structural failure. To ensure that there are no observable construction defects in newly built homes bought by FHA-insured borrowers, HUD is retaining the requirement that the Warranty of Completion of Construction (form HUD-92544) be executed by the builder and the buyer of the home, as a condition for FHA mortgage insurance. In addition, the rule requires that inspections be performed by qualified individuals, to further mitigate risk. If all these safeguards fail, then HUD estimates that the average aggregate loss to FHA (a transfer of risk) is \$1.3 million, which is far below the consumer benefits generated by the rule.

Paperwork Reduction Act

The information collection requirements contained in this rule have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB Control Numbers 2502-0059 (Warranty of Completion of Construction (form HUD-92544)). In accordance with the Paperwork Reduction Act, an agency 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.

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. As noted above in this preamble, this rule is a deregulatory action taken by HUD that will alleviate the economic costs borne by participants in the FHA single family mortgage insurance programs. As discussed in this preamble, removal of the requirement for a 10-year protection plan would ease burdens on lenders and homebuilders and does not preclude borrowers from purchasing such plans. HUD is removing this requirement because it has deemed they are no longer necessary. Therefore, the undersigned certifies that this rule will not have a significant impact on a substantial number of small entities.

Environmental Impact

This rule does not direct, provide for assistance or loan and mortgage insurance for, or otherwise govern or regulate, real property acquisition, disposition, leasing, rehabilitation, alteration, demolition, or new construction, or establish, revise, or provide for standards for construction or construction materials, manufactured housing, or occupancy. In addition, part of this rule changes a statutorily required and/or discretionary establishment and review of loan limits. Accordingly, under 24 CFR 50.19(c)(1) and (c)(6), this rule is categorically excluded from environmental review under the National Environmental Policy Act of 1969 (42 U.S.C. 4321).

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 or 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 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 Executive 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 rule does not impose any federal mandates on any State, local, or tribal governments, or on the private sector, within the meaning of UMRA.

Catalogue of Federal Domestic Assistance

The Catalogue of Federal Domestic Assistance Number for the principal FHA single-family mortgage insurance program is 14.117.

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 discussed in the preamble, HUD amends 24 CFR part 203 to read as follows:

PART 203 – SINGLE FAMILY MORTGAGE INSURANCE

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

Authority: 12 U.S.C. 1709, 1710, 1715b, 1715z-16, and 1715u; 42 U.S.C. 3535(d).

§ 203.18 [Amended]

2. In § 203.18, remove paragraph (a)(3) and redesignate paragraph (a)(4) as paragraph (a)(3).

3. In § 203.50, revise paragraph (f)(1) to read as follows:

§ 203.50 Eligibility of rehabilitation loans.

* * * * *

(f) * * *

(1)(i) The limits prescribed in § 203.18(a)(1) (in the case of a dwelling to be occupied as a principal residence, as defined in § 203.18(f)(1));

(ii) The limits prescribed in § 203.18(a)(1) and (3) (in the case of a dwelling to be occupied as a secondary residence, as defined in § 203.18(f)(2));

(iii) 85 percent of the limits prescribed in § 203.18(c), or such higher limit, not to exceed the limits set forth in § 203.18(a)(1), as Commissioner may prescribe (in the case of an eligible non-occupant mortgagor as defined in § 203.18(f)(3));

(iv) The limits prescribed in § 203.18a, based upon the sum of the estimated cost of rehabilitation and the Commissioner's estimate of the value of the property before rehabilitation;

or

* * * * *

§§ 203.200 through 203.209 [Removed]

4. Remove the undesignated center heading “Insured Ten-Year Protection Plans (Plan)” and §§ 203.200 through 203.209.

Dated: December 3, 2018

Brian D. Montgomery
Assistant Secretary for Housing – Federal
Housing Commissioner

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