U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

Date: May 2, 2023

Mortgagee Letter 2023-09

To: All FHA-Approved Mortgagees
All Direct Endorsement Underwriters
All Eligible Submission Sources for Condominium Project Approvals
All FHA Roster Appraisers
All FHA-Approved 203(k) Consultants
All HUD-Approved Housing Counselors
All HUD-Approved Nonprofit Organizations
All Governmental Entity Participants
All Real Estate Brokers
All Closing Agents

Subject

Adjustable-Rate Mortgages (ARM): New Secretary-Approved Interest Rate Indices and Requirements for Transitioning from the London Interbank Offered Rate (LIBOR) Index

Purpose

This Mortgagee Letter (ML) implements the provisions of Final Rule, *Adjustable Rate Mortgages: Transitioning from LIBOR to Alternative Indices* (Docket No. FR-6151-F-03) (Final Rule).

Effective Date

The policy requirements in this Mortgagee Letter are effective as follows:

Section of ML	Effective Date
Forward Mortgages	
Section 251 Adjustable Rate Mortgages (II.A.8.f.v) – Indices	Effectively Immediately.
Transitioning existing LIBOR-indexed Forward ARMs to the Secretary-approved Replacement Index	The next interest rate adjustment date on or after the first London banking day after June 30, 2023.[1]

[1] If the Board of Governors of the Federal Reserve System declares that a LIBOR tenor will cease to be published or will become unrepresentative, then the effective date is the first business day following the date announced by the Board of Governors.

Section of ML	Effective Date
Home Equity Conversion Mortgages (HECM)	
Transitioning Existing LIBOR-indexed Adjustable Rate HECMs to the Secretary-approved Replacement Index	The next interest rate adjustment date on or after the first London banking day after June 30, 2023.[1]
New Originations of Adjustable Rate HECMs	Effective Immediately.
HECM Interest Rate Index Floor for New Originations	Effective Immediately.
Monthly Adjustable Rate HECMs – Maximum Mortgage (Note) Interest Rate	Effective Immediately.
Changes to HECM Model Notes	Mortgagees may begin using the newly revised HECM Model Note immediately. Mortgagees must use the revised Model Note for all case numbers assigned on or after July 1, 2023.

All updates will be incorporated into a forthcoming update of the HUD Handbook 4000.1, *FHA Single Family Housing Policy Handbook* (Handbook 4000.1).

Public Feedback

HUD welcomes feedback from interested parties for a period of 30 calendar days from the date of issuance. To provide feedback on this policy document, please send feedback to the FHA Resource Center at answers@hud.gov or call 1-800-CALLFHA (1-800-225-5342). HUD will consider the feedback in determining the need for future updates.

Affected Programs

The provisions of this ML apply to all Single Family Title II programs, including the HECM program.

Background

In July of 2017, the United Kingdom's Financial Conduct Authority (FCA), the financial regulator of LIBOR, announced that it would no longer persuade or compel contributing banks to submit rates used to calculate LIBOR after December 31, 2021. On March 5, 2021, the Intercontinental Exchange (ICE) Benchmark Administration Limited (IBA) published the feedback it received to its December 2020 report on the potential cessation of LIBOR, and announced it intended to cease publication of the overnight and 1, 3, 6, and 12 month USD LIBOR immediately following the LIBOR publication on June 30, 2023.

Congress passed the Adjustable Interest Rate (LIBOR) Act of 2021 (LIBOR Act) as part of the Consolidated Appropriations Act, 2022 (Pub. L. 117-103) to, in part, create a clear and uniform process, on a nationwide basis, for replacing LIBOR in existing contracts where the terms do not provide for the use of a clearly defined or practicable replacement benchmark rate, without affecting the ability of parties to use any appropriate benchmark rate in a new contract. Generally, for existing LIBOR-based ARMs without language providing for a specific replacement index, the default replacement index will be a spread adjusted term rate based on the Secured Overnight Financing Rate (SOFR), as provided under the LIBOR Act.

The Alternative Reference Rate Committee (ARRC) is a group of private-market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York to help ensure a successful transition from U.S. dollar (USD) LIBOR to a more robust reference rate. In its Best Practices last updated on April 21, 2023, the ARRC recommended the use of the Refinitiv USD IBOR Consumer Cash Fallback based on the Chicago Mercantile Exchange (CME) Group's Term SOFR rates (CME Term SOFR) plus the applicable spread adjustment for legacy LIBOR ARMs and the use of SOFR averages for new originations.

On October 19, 2022, HUD published a proposed rule in the Federal Register (FR). After reviewing and considering the comments received, HUD published the Final Rule in the FR on March 1, 2023, to revise its regulations in parts 203 and 206. This ML implements the Final Rule and establishes the All-In CME Term SOFR, which includes the applicable spread adjustment, as published by Refinitiv Benchmark Services (UK) Limited, as the Secretary-approved replacement Index.

HUD previously provided Mortgagees updated instructions on FHA-specific modifications for forward mortgage and HECM model loan documents that includes fallback language for future adjustable interest rate index transition events, as described in ML 2021-08 for HECMs, superseded by this ML, and in ML 2023-01 for forward mortgages.

Summary of Changes

This ML:

- updates Handbook 4000.1, Section 251 Adjustable Rate Mortgages – Indices (II.A.8.f.v);
- adds Interest Rate Transition from LIBOR Index to SOFR Index (Handbook 4000.1, III.A.3.a.ii(A)), and renumbers subsequent sections;
- adds new policy for Transitioning Existing LIBOR-indexed Adjustable Rate HECMs to the Secretary-approved Replacement Index;

- provides updated policy for interest rate adjustments on existing ARMs and supersedes where it conflicts in Handbooks 4235.1, REV-1 and 4330.1, REV-5;
- updates policy for New Originations of Adjustable Rate HECMs and supersedes in its entirety ML 2021-08, Home Equity Conversion Mortgage (HECM) Program – Changes to Interest Rate Requirements Including Removal of the London Interbank Offered Rate (LIBOR) Index;
- establishes a Monthly Adjustable HECM maximum Mortgage Note Interest Rate; and,
- provides Mortgagees the FHA specific modifications made to the HECM first and second notes found at: https://www.hud.gov/program_offices/housing/sfh/model_documents.

FHA Single Family Housing Policy Handbook 4000.1

Origination Through Post-Closing/ Endorsement

The policy changes will be incorporated into Handbook 4000.1 as follows:

Programs and Products - Section 251 Adjustable Rate Mortgages (II.A.8.f)

v. Indices

The interest rate governing index may be the 1-Year Constant Maturity Treasury (CMT) or 30-day average Secured Overnight Financing Rate (SOFR).

The 1-Year CMT is the weekly average yield on U.S. Treasury Securities, adjusted to a constant maturity of one year, as published by the Board of Governors of the Federal Reserve System in its statistical release on Selected Interest Rates (H.15) at https://www.federalreserve.gov/releases/h15/default.htm.

The 30-day average SOFR is the compounded average of the SOFR over a rolling 30-day period, as administered and published daily by the Federal Reserve Bank of New York and available at: https://www.newyorkfed.org\markets\reference-rates\sofr-averages-and-index.

FHA Single Family Housing Policy Handbook 4000.1

Servicing and Loss Mitigation

Adjustable Rate Mortgages (III.A.3.a)

i. Definitions

The Change Date is the effective date of an adjustment to the interest rate, as shown in Paragraph 4(A) of the model Adjustable Rate Note form.

The Initial Index Figure is the most recent figure available before the Closing Date of the Mortgage.

The Current Index Figure is:

- the most recent index figure available 30 Days before the date of each interest rate adjustment, for Mortgages closed before January 10, 2015; and
- the most recent figure available 45 Days before the date of each interest rate adjustment, for Mortgages closed on or after January 10, 2015.

ii. Adjusting the Interest Rate on an ARM

To set the new interest rate on an ARM annually, the Mortgagee must review the mortgage documents containing interest rate provisions, and:

- determine the change between the Initial Index Figure and the Current Index Figure; or
- add a specified margin to the Current Index Figure.

Once the new adjusted interest rate is calculated, the Mortgagee must provide notice of the change to the Borrower.

(A) Interest Rate Transition from LIBOR Index to SOFR Index

For adjustable interest rate Mortgages indexed to the London Interbank Offered Rate (LIBOR), Mortgagees must transition the Mortgage from LIBOR to the applicable Refinitiv United States Dollar (USD) IBOR Consumer Cash Fallback (Refinitiv) Secretary-approved spread-adjusted Chicago Mercantile Exchange (CME) Term SOFR tenor replacement index as indicated in the table below to calculate the periodic adjustments to the mortgage interest rate:

Existing FHA-Insured LIBOR-indexed Forward ARM	**Secretary-Approved Replacement Index**
1-, 3-, 5-, 7-, 10-Year Forward ARMs	12-Month CME Term SOFR (Refinitiv Instrument Code USDCFCFCTSA1Y=)
The approved Refinitiv 12-month CME Term SOFR replacement index is found at: https://www.refinitiv.com/en/financial-data/financial-benchmarks/usd-ibor-cash-fallbacks. **Note:** When downloading historical SOFR rates from Refinitiv, Mortgagees must use the "All-In" CME Term SOFR Rate and select the "Feature" (No Floor).	

The Mortgagee must include a notification to the Borrower of the transition from the LIBOR index to the 12-Month CME Term SOFR replacement index in the ARM Adjustment Notice in accordance with the mortgage documents (III.A.3.a.iv).

The Mortgagee must calculate the interest rate for each subsequent adjustment to the Mortgage using the 12-Month CME Term SOFR replacement index.

Transitioning Existing LIBOR-indexed Adjustable Rate HECMs to the Secretary-approved Replacement Index

For adjustable interest rate HECMs indexed to the LIBOR, Mortgagees must transition the Mortgage from LIBOR to the Secured Overnight Financing Rate (SOFR) index by using the applicable Refinitiv USD IBOR Consumer Cash Fallback (Refinitiv) spread-adjusted CME Term SOFR tenor replacement index as indicated in the table below to calculate the periodic adjustments to the mortgage interest rate.

Existing FHA-Insured LIBOR-indexed Adjustable Rate HECMs	**Secretary-Approved Replacement Index**
Annually Adjustable Rate HECMs	12-Month CME Term SOFR (Refinitiv Instrument Code USDCFCFCTSA1Y=)
Monthly Adjustable Rate HECMs	1-Month CME Term SOFR (Refinitiv Instrument Code USDCFCFCTSA1M=)
The approved Refinitiv USD IBOR Consumer Cash Fallback (Refinitiv) CME Term SOFR tenor replacement indices are found at: https://www.refinitiv.com/en/financial-data/financial-benchmarks/usd-ibor-cash-fallbacks. **Note:** When downloading historical SOFR rates from Refinitiv, Mortgagees must use the "All-In" SOFR Rate and select the "Feature" (No Floor).	

Periodic Adjustment Lookback Period

The current index for periodic adjustments is the index in effect 30 days before the interest rate Change Date, as provided in the Note.

The Mortgagee must use the rate published on the first business day of each week and which is in effect 30 days before the interest rate Change Date. The rate is effective the next day after the index is published. The rate remains in effect until the subsequent rate becomes effective the following week. The published Refinitiv CME Term SOFR index must be rounded to three digits to the right of the decimal point.

Initial Periodic Adjustment Interest Rate Calculation

The Mortgagee must calculate the periodic adjustment to the interest rate as the sum of the applicable Refinitiv CME Term SOFR Index tenor plus the margin set at origination, in accordance with the terms of the Note and FHA requirements.

Borrower Notice

Mortgagees must provide the Borrower with a Notice of Interest Rate Change at least 25 days before the next periodic adjustment and include:

- the Change Date;
- the new mortgage interest rate;
- the current Refinitiv CME Term SOFR index value used to calculate the new interest rate; and
- the publication date of the Refinitiv CME Term SOFR index applicable to the periodic adjustment, as determined by the Periodic Adjustment Lookback Period.

New Originations of Adjustable Rate HECMs

Mortgagees must comply with the index requirements in the table below.

<table>
<tr><th colspan="3">Eligible Index Types</th></tr>
<tr><th>Adjustable Rate Types</th><th>Expected Average Mortgage Interest Rate</th><th>Initial Note Rate and Periodic Adjustments</th></tr>
<tr><td rowspan="2">Annually Adjustable</td><td rowspan="2">10-Year CMT</td><td>1-Year CMT</td></tr>
<tr><td>30-Day Average SOFR</td></tr>
<tr><td rowspan="2">Monthly Adjustable</td><td rowspan="2">10-Year CMT</td><td>1-Year CMT</td></tr>
<tr><td>1-Month CMT</td></tr>
<tr><td colspan="3">The expected average mortgage interest rate means the interest rate used to calculate the principal limit established at closing. The expected average mortgage interest rate is the sum of the Mortgagee’s margin plus the weekly average yield for U.S. Treasury securities (CMT) adjusted to a constant maturity of 10 years.</td></tr>
</table>

Establishing the Secured Overnight Financing Rate (SOFR) Index

The Federal Reserve Bank of New York publishes the 30-day average SOFR index each business day on their website at: https://apps.newyorkfed.org/markets/autorates/sofr-avg-ind. The Mortgagee must use the rate published on the first business day of each week and which is in effect the next day after the index is published. The rate remains in effect until the subsequent index rate becomes effective the following week. The published 30-Day Average SOFR index figure shall be rounded to three digits to the right of the decimal point.

HECM Interest Rate Index Floor for New Originations

For all new HECM originations, the index value used to determine the initial Note rate and periodic adjustments must not be below zero. In the event the current index for an adjustable interest rate HECM falls below zero, the current index will be deemed to be zero for purposes of calculating the borrower's Note rate.

Monthly Adjustable HECMs – Maximum Mortgage (Note) Interest Rate

The Mortgagee may only offer a monthly adjustable rate HECM when the Mortgagee also offers an annually adjustable rate HECM. The maximum lifetime Note rate may not be more than ten percent higher than the initial Note rate.

Periodic adjustments in the Note rate must correspond to the upward and downward change in the index, except that downward changes in the current index will not result in an index figure that is less than zero.

Changes to HECM Model Notes

FHA has revised the model loan documents for the first and second HECM Adjustable Interest Rate Notes to be consistent with the Final Rule and this ML.

The revised model loan documents are accessible from the following website: https://www.hud.gov/program_offices/housing/sfh/model_documents.

Mortgagees are reminded they are responsible for adapting model documents to ensure compliance with other federal, state, and local laws, and may do so without HUD approval.

Paperwork Reduction Act

The information collection requirements contained in this document have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. 3501-3520) and assigned OMB control numbers 2502-0005; 2502-0059; 2502-0117; 2502-0189; 2502-0302; 2502-0306; 2502-0322; 2502-0328; 2502-0358; 2502-0404; 2502-0414; 2502-0429; 2502-0494; 2502-0496; 2502-0524; 2502-0525; 2502-0527; 2502-0538; 2502-0540; 2502-0556; 2502-0561; 2502-0566; 2502-0570; 2502-0583; 2502-0584; 2502-0589; 2502-0595; 2502-0600; 2502-0610; and 2502-0611. In accordance with the PRA, 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.

Questions

Any questions regarding this ML may be directed to the FHA Resource Center at 1-800-CALLFHA (1-800-225-5342), answers@hud.gov, or www.hud.gov/answers. The FHA Resource Center is prepared to accept calls from persons who are deaf or hard of hearing, as well as individuals with speech or communication disabilities. Information on how to make an accessible phone call is available at https://www.fcc.gov/consumers/guides/telecommunications-relay-service-trs.

Signature

Julia R. Gordon
Assistant Secretary for Housing -
FHA Commissioner