January 19, 2026

The Honorable Frank Cassidy
Assistant Secretary for Housing, Federal Housing Commissioner
Department of Housing and Urban Development
451 7th St., S.W.
Washington, D.C. 20410

RE: Draft Mortgagee Letter: Use of Independent Third-Party Providers in Connection with Claims Without Conveyance of Title (CWCOT)

Dear Commissioner Cassidy:

On behalf of the clients and communities we represent, we write to comment on the Draft Mortgagee Letter, "Use of Independent Third-Party Providers in Connection with Claims Without Conveyance of Title (CWCOT)," posted on the Single Family Housing Drafting Table on December 4, 2025.

We urge FHA to retain the current language in Handbook 4000.1 that prevents "Mortgagees" from contracting with any affiliates, subsidiaries, or similarly situated companies in the conduct of foreclosure sales.[1] HUD has proposed draft language to apply the ban only to "Mortgage Holders," which would allow "Mortgage Servicers" to use affiliates to conduct foreclosure sales. Unfortunately, the distinction between Mortgage Holder and Mortgage Servicer does not ameliorate the concerns that this language is intended to address. The proposed relaxation of the ban on the use of affiliates in foreclosure sales would create unnecessary financial risks to the Mutual Mortgage Insurance (MMI) Fund and cause unintended consequences for FHA borrowers due to a shift in incentives for mortgage servicers.

We see three significant financial risks to the MMI Fund from this proposed change:

1. It incentivizes foreclosure over cost-saving home retention options.

2. It incentivizes foreclosures over cost-saving home disposition options.

3. It could result in lower sales prices from foreclosure auctions.

---

[1] U.S. Dep't of Hous. & Urban Dev., 4000.1: FHA Single Family Housing Policy Handbook, at III(A)(2)(p)(iii)(D)(1) (Nov. 26, 2025).

We describe each of these risks in more detail below.

First, the proposal creates an unnecessary financial risk to the MMI Fund by creating a financial incentive toward foreclosure over cost-saving home retention options. In Handbook 4000.1, HUD recognizes that financial incentives have an important impact on the loss mitigation process. Rather than relying only on the mandatory nature of the waterfall, HUD pays Mortgagees up to $200 for executing a Partial Claim, $750 plus up to $250 in fees for a Loan Modification, and $1,750 for a Payment Supplement.[2] The apparent reason that the affiliated business rule at issue was first established was because HUD recognized that having a significant business relationship with a foreclosure auction provider could create an incentive for Mortgagees to prefer foreclosure over loss mitigation and therefore not have a strong enough incentive to put their best efforts into the mandatory loss mitigation waterfall. The misalignment of incentives between servicers and holders was a significant driver of issues that led to the foreclosure crisis that started in 2008.

In considering the potential misalignment of incentives, it is important to understand that the fees for conducting the foreclosure are substantially higher than the incentive fees paid to servicers for home retention. Under current HUD policy, the fees that HUD reimburses from a foreclosure sale are between 3-5% of the Unpaid Principal Balance of the loan at issue.[3] For an average delinquent FHA loan of $257,000, a 3% fee is $7,710 and a 5% fee is $12,850. This means that for almost all FHA loans, the foreclosure fee would be significantly higher than the incentive payments available for completing any of the home retention options.

The draft Mortgagee Letter seeks to address the potential of misaligned incentives by stating, without supporting evidence, that “the concerns regarding a Mortgagee’s influence or a conflict of interest with a Third Party Provider is more appropriate when focused on the Mortgage Holder” as opposed to the Mortgage Servicer.[4] We disagree, because the Mortgage Servicer has the same conflict as the Mortgage Holder, if not more of a conflict. In a situation where the Mortgage Holder and the Mortgage Servicer are different entities, the Holder is not making loan-level decisions whether to pursue home retention or foreclosure, but rather the Mortgage Servicer is. The Mortgage Servicer, not the Mortgage Holder, interacts with the borrower, and under the revised waterfall, decides the appropriate loss mitigation option based on the conversation with the borrower. It is the Mortgage Servicer that guides the borrower through the home retention process and determines what option is appropriate. Consequently, it is most important for FHA to property incentivize the activity of the Mortgage Servicer, although incentives are also clearly important for the Holder as well. HUD should therefore focus on Mortgage Servicer’s influence and potential conflicts of interest.

Like FHA, the GSEs recognize the potential risk of improperly aligned monetary incentives driving servicer behavior. According to Fannie Mae’s Servicing Guide A4-2.2-03,

---

[2] *Id*. at III(A)(2)(k)(i).
[3] *Id*. at III(A)(2)(p)(iii)(D)(1).
[4] U.S. Dep’t of Hous. & Urban Dev, Draft Mortgagee Letter - Use of Independent Third-Party Providers in Connection with Claims Without Conveyance of Title (CWCOT) at pg. 2.

"[a]rrangements with vendors and other service providers, particularly affiliates, must not be influenced by an actual or perceived conflict of interest. The servicer and law firm must use the most cost-efficient and effective vendors to assist in processing foreclosures and bankruptcy cases without regard to arrangements that could provide a financial benefit directly or indirectly to the servicer."[5] While the GSEs rather than the servicers select the auction vendor, so they are not similarly situated to FHA with respect to auction vendors, it is clear that they consider the servicer to be the decisionmaker whose incentives need to be considered.

Properly incentivizing home retention actions under the waterfall is particularly important because they save the MMI Fund a substantial amount of money. A September 2025 paper published by the Housing Policy Council, "Quantifying the Savings from FHA's Home Retention Programs," demonstrates that home retention options through FHA's waterfall save the Fund around $25,000 on average per seriously delinquent loan as compared to a disposition.[6] Given the effectiveness of the waterfall, it is crucially important for FHA to ensure that Mortgage Servicers are fully incentivized to follow it. Moreover, home retention options stabilize homeownership for the borrowers that the program is designed to serve, and they promote stable and healthy neighborhoods.

We are not claiming that HUD's proposed change will automatically cause servicers employing their own auction provider to ignore the Handbook requirements for home retention. Instead, we believe that the proposed change creates a significant risk that the servicer will place less emphasis on home retention because of the economic incentive it creates toward foreclosure. We urge HUD to eliminate this sizeable risk by returning to previous language that avoids it.

Second, the proposal risks creating a financial incentive toward foreclosure over FHA's home disposition options. As with home retention, HUD pays incentives for its home disposition options ($1,000 for a pre-foreclosure sale and $250 for a deed in lieu of foreclosure), and these payments are substantially lower than the current fees from conducting a foreclosure sale.[7] And, as with home retention, it is the Mortgage Servicer that processes the request for FHA Loss Mitigation Disposition options and is the entity that HUD should properly incentivize. We are significantly concerned that HUD's proposed policy also increases the risk that Mortgage Servicers fail to properly evaluate Home Disposition options. HUD has created these disposition options because, first and foremost, they save money for the MMI Fund. Additionally, they save money for borrowers who don't have to pay foreclosure fees and costs; they encourage the quicker return of homes to the housing supply; and they prevent the neighborhood blight that often results when homes go through a lengthy foreclosure process. For all these reasons, HUD should ensure they are properly incentivized and used to the benefit of the MMI fund and FHA-insured borrowers.

---

[5] Fannie Mae Single-Family Servicing Guide, at A4-2.2-03, Prohibition Against Servicer-Specified Vendors for Fannie Mae Referrals, Use of Vendors, and Outsourcing Companies (Apr. 12, 2017).
[6] Kanav Bhagat, Housing Policy and Risk Advisors, "Quantifying the Savings from FHA's Home Retention Programs," Housing Policy Council Research Papers (Sept. 2025).
[7] U.S. Dep't of Hous. & Urban Dev., 4000.1: FHA Single Family Housing Policy Handbook, at III(A)(2)(k)(1) (Nov. 26, 2025).

The risk of Mortgage Servicers skipping over disposition options is even more concerning because these options involve borrowers who may already have accepted the need to move from their home. Some borrowers, especially those with representation or assistance from a counselor, will be persistent when it comes to seeking home retention options; however, when borrowers are already resigned to losing their homes, they may be much less likely to push hard for a disposition option. This lack of borrower persistence makes it more likely that cost-saving FHA disposition options would be skipped.

Third, the proposed rule risks lower sales prices from foreclosure auctions, which also hurts the MMI Fund. HUD's data show that even after periods of significant housing price appreciation, HUD still loses money on foreclosures and related home dispositions. According to HUD's recent report, the loss rate for REO in Quarter 2 of 2025 is 39.76% and for REO Alternatives, including CWCOT, it is 22.17%.[8] For CWCOT, FHA's loss severity depends on the ability of the auction providers that servicers select to obtain the highest price and conduct the fastest sale. The sale price and time to sale depend on how quickly and effectively the auction companies are able to market the property and conduct the sale, which require investments in technology and business processes. Therefore, HUD has a clear economic interest in ensuring a competitive and efficient foreclosure sale process.

To ensure a competitive process, HUD should make sure that auction vendors are chosen because of their effectiveness and not because of a business relationship with and fees potentially accruing to the entity choosing the vendor, whether it be a Holder or a Mortgage Servicer. If HUD proceeds with its policy change, it will create the risk that the deciding factor in selecting vendors is the financial benefit from the house sale rather than performance of faster sales at higher prices, which would lead to greater losses to Fund. The only way that FHA can avoid this risk is to maintain the third-party requirement currently in place for Mortgage Servicer selection of auction providers.

We urge HUD to maintain its current policy because the proposed revision imposes unnecessary risks to the MMI Fund. If you have any questions about this letter or would like to meet with us about it, please contact Steve Sharpe, Senior Attorney at the National Consumer Law Center at ssharpe@nclc.org.

Thank you for the opportunity to comment.

Sincerely,

Center for Responsible Lending
National Consumer Law Center (on behalf of its low-income clients)

---

[8] U.S. Dep't of Hous. & Urban Dev, Quarterly Report to Congress on the Federal Housing Administration Single Family Mutual Mortgage Insurance Fund at Ex. A-7 (Quarter 2, Fiscal Year 2025).