58.10: Insurance loss settlements (08/21/06)

Upon notification of loss or damage to the Mortgaged Premises, the Servicer must monitor and coordinate the claim process with the Borrower and the insurer. The Servicer must take appropriate action to:

- Verify the extent of the loss or damage
- Ensure judicious disbursement of insurance proceeds for the necessary repairs
- Protect the priority of the Mortgage by obtaining, where necessary, waivers of materialman's or mechanic's liens
- Document completion of the repairs

Refer to Section 67.27, Servicing Mortgages on distressed properties, for additional requirements.

The Servicer may be named as loss payee on insurance drafts and must comply with any applicable law and, where applicable, any requirement of the FHA, VA, RHS or MI. Details concerning the loss or damage and disposition of the insurance proceeds must be recorded in the Mortgage file.

The Servicer need not submit a report and related recommendations to Freddie Mac unless:

- The Mortgage is in foreclosure or the Mortgaged Premises have been acquired by the Servicer through foreclosure or deed-in-lieu of foreclosure (See Section 70.16(b) for remittance requirements for insurance loss settlements.)
- The insured improvements have suffered a total or near total loss
- The Servicer wishes to apply insurance proceeds to the Mortgage debt instead of repairing the property, or
- Insurance proceeds exceed the amounts required to restore the property to its original condition

If any of the above conditions exist, the Servicer must submit the recommendation along with the appropriate documentation to us **(see Directory 5)** via Form 105, within five Business Days of learning of the situation.

Following is guidance to assist the Servicer in satisfying the requirements of this section.

(a)

Property insurance claims

Property insurance that Freddie Mac requires the Borrowers to maintain should provide sufficient recoveries for losses or damages to the Mortgaged Premises:

- **Loss-of-use or additional living expense clause:** Homeowner insurance policies generally have a loss-of-use or additional living expense clause. This clause covers increases in living expenses necessary for an insured household to:
  - Maintain its normal living standards away from a residence that is being repaired or reconstructed
  - Permanently resettle elsewhere

- **Claim proceeds:** Insurers generally issue drafts directly to the insured Borrower in payment for losses to contents (as opposed to structural losses) or for off-residence living expenses. If any such payment is made jointly to the Borrower and the Servicer, the Servicer must release the insurance funds to the Borrower without delay.

  When an insurance draft for structural losses is payable jointly to the insured Borrower and the Servicer, the Servicer may immediately release insurance funds to Borrowers who legitimately need to advance funds to contractors, provided all of the following conditions are met:

  - The Mortgage is current.
  - The Borrower's payment history does not show delinquencies of two payments or more.
  - The released funds do not exceed the highest of:
    - $10,000.00
    - 10% of the unpaid principal balance (UPB) of the affected Mortgage
    - The amount by which the released funds exceed the UPB of the Mortgage

  When the amount of insurance funds released equals or exceeds $10,000, the Servicer must have the Borrower execute an affidavit in which the Borrower expressly agrees to apply the released funds promptly to repair or reconstruct the residence.

  A Servicer may unilaterally apply the insurance proceeds to the Mortgage's unpaid balance only to the extent allowed by applicable law and the Security Instrument. The Borrower, however, may unilaterally decide to have the proceeds applied to the Mortgage's unpaid balance.

  If repair or reconstruction of the residence is expected to take more than three months, insurance funds retained by the Servicer pending disbursement for such repair or reconstruction must be maintained in a federally insured account that pays interest to the Borrower.

(b) Repair or reconstruction of the Mortgaged Premises

In overseeing the repair or reconstruction of damaged or destroyed residences, the Servicer should, to the extent applicable and practicable, ascertain that:

- The contractor chosen by the Borrower to repair or reconstruct the residence is:
  - Duly licensed under applicable laws and regulations
  - Qualified and experienced to perform the types of work contracted
  - Financially able to complete the repair or reconstruction within scheduled timeframes
- The plans and specifications for the work contracted:
  - Describe repair or reconstruction that is generally consistent with the damage or destruction suffered by the residence, as reported in the proof of loss filed by the Borrower with the property insurer and as documented by the insurer's adjuster
  - Establish a reasonable schedule for completion of each phase of repair or reconstruction
- The Borrower and the contractor have executed a contract by which they agree to the following:

- The contractor will perform the work described in the plans and specifications.
- The contractor will comply with applicable codes and regulations governing residential repair or reconstruction (including, but not limited to, building codes and zoning, permit and inspection regulations):
  - These codes and regulations may vary from State to State and, within the same State, from county to county. Therefore, Servicers should have adequate measures in place to verify contractors' and inspectors' compliance certifications to protect Freddie Mac's and the Servicer's respective investments.

    If additional funds are needed to bring a damaged or destroyed residence into compliance with applicable codes and regulations, the Borrowers should determine whether their property insurer will waive any policy provision restricting payment for the increased cost of construction resulting from enforcement of codes and regulations.
- A specified dollar amount is the maximum amount that the contractor may charge for the work.
- The contractor will be paid a specified advance (if applicable, usually not exceeding 10 percent of the total contract amount) and, subsequently, on a specified draw schedule contingent on verification of satisfactory completion of specified work phases.
- The contractor, its subcontractors and its material suppliers will provide written acknowledgment of payment for work performed and materials supplied and the necessary lien waivers or releases so that the Mortgaged Premises may remain clear of all such liens and encumbrances.

- Each scheduled work phase has been satisfactorily completed in accordance with the plans and specifications before disbursement of payment for such phase is made in accordance with the contract

The Servicer may choose to have the above described oversight functions performed by its staff or by a third party (such as a specialized firm or another Servicer). However, the Servicer is liable for the performance of any third party it retains. The third party may be compensated from insurance proceeds retained by the Servicer only to the extent agreed to by the Borrower and allowed under applicable law.