Veterans Benefits Administration
Department of Veterans Affairs
Washington, D.C. 20420

Circular 26-19-22
Exhibit B
August 8, 2019

Determining Recoupment Period for IRRRLs

To determine the recoupment period for IRRRLs, divide the sum of all incurred fees, expenses, and closing costs, whether included in the loan or paid outside of closing, by the reduction of monthly principal and interest (PI) payment. Lender credits may be used to offset allowable fees and charges.

$$\frac{\text{(Fees + Expenses + Closing Costs) - Lender Credit}}{\text{Reduction of Monthly PI Payment}} \leq \text{36 months}$$

As a reminder, lenders do not need to complete the statutory recoupment calculation explained below *unless the recoupment period shown on the final loan disclosure outlined in paragraph 3.d.(2) of this Circular is more than 36 months*.

Fees, Expenses, and Closing Costs (FECC) to be Recouped

Refer to the below table for information about specific fees and charges to be included in or excluded from the recoupment calculation. *Please continue to refer to Chapter 8 of VA Lenders Handbook (M26-7) for information about allowable fees, expenses, and closing costs.*

Included FECC	Excluded FECC

• Allowable fees and charges
  − Included in the loan amount
  − Paid outside of closing
• Credit report (if required)
• Appraisal fee[1] (if applicable and the lender requires Veteran to pay)
• Reasonable discount points
  − Included in the loan amount
  − Paid outside of closing
 	
Note: Lender credits may be used to offset allowable fees and charges (including discount points).
	• VA funding fee
	• Per diem interest
	• Escrow
	• Prepaid expenses
	  − Insurance
	  − Taxes (including delinquent taxes)
	  − Special assessments
	  − Homeowners' association (HOA) fees
	
	Note: This is not an all-inclusive list of prepaid expenses.

[1] The Veteran may only be charged a reasonable and customary amount, and only charged for one appraisal.

Calculating the Monthly PI Reduction

For purposes of calculating the recoupment period, 38 U.S.C. § 3709(a)(3) allows lenders to exclude taxes, amounts held in escrow and fees paid under chapter 37, title 38, U.S.C., from the calculation. As such, when determining the reduction in monthly payment for the new loan, the lender may exclude these from the monthly PI calculation.

Example of a Fixed-to-Fixed Recoupment Calculation

	Original Loan	New Loan
Total Loan Amount	$610,000	$608,025
Included FECC Added to Loan	N/A	$6,500
Included FECC Paid Outside of Closing	N/A	$436.49
Funding Fee Added to Loan	N/A	$3,025
Prepaid Expenses	N/A	$6,000
Monthly PI	$3,090.78	$2,902.68
Monthly PI (when funding fee is subtracted from Total Loan Amount)	N/A	$2,888.36
Loan Type	Fixed	Fixed
Loan Term	30 years	30 years
Interest Rate	4.50%	4.00%

Recoupment calculated with the funding fee and prepaid expenses in Monthly PI:
$6,936.49 (fees/expenses/closing costs) ÷ $188.10 (PI reduction) = 37 months (36.88 months rounded up to the nearest month) Does not meet 36-month recoupment requirement.

Recoupment calculated without funding fee and prepaid expenses in Monthly PI:
$6,936.49 (fees/expenses/closing costs) ÷ $202.42 (PI reduction) = 35 months (34.27 months rounded up to the nearest month) Meets 36-month recoupment requirement.

If a Veteran is refinancing with an **Energy Efficient Mortgage (EEM),** the EEM amount, while generally held in escrow, is not a fee, closing cost, or expense, as contemplated under 38 U.S.C. § 3709(a). Therefore, it is not included as an amount to be recouped. VA acknowledges that in most cases the additional monies added to the Total Loan Amount for the energy efficient improvement will make it difficult, if not impossible, to meet the 36-month recoupment calculation. Because the intent of the EEM is to “pay for itself,” VA will allow lenders to subtract the EEM amount from the Total Loan Amount when determining Monthly PI for purposes of calculating statutory recoupment. Lenders must still include the EEM amount when providing the loan comparison statement to the Veteran. An example is provided below.

Example of a Fixed-to-Fixed with EEM Recoupment Calculation

	Original Loan	New Loan
Total Loan Amount	$140,000	$135,000
Included FECC Added to Loan	N/A	$2,500
Included FECC Paid Outside of Closing	N/A	$436.49
EEM Amount	N/A	$6,000
Monthly PI	$709.36	$644.51
Monthly PI (when EEM Amount is subtracted from Total Loan Amount)	N/A	$615.87
Loan Type	Fixed	Fixed
Loan Term	30 years	30 years
Interest Rate	4.50%	4.00%

Recoupment calculated with EEM Amount in Monthly PI:

$2,936.49 (fees/expenses/closing costs) ÷ $64.85 (PI reduction) = 46 months (45.28 months rounded up to the nearest month) Does not meet 36-month recoupment requirement.

Recoupment calculated without EEM Amount in Monthly PI:

$2,936.49 (fees/expenses/closing costs) ÷ $93.49 (PI reduction) = 32 months (31.41 months rounded up to the nearest month) Meets 36-month recoupment requirement.

Recoupment Calculation Examples

Example of a Fixed-to-Fixed Recoupment Calculation

	Original Loan	New Loan
Total Loan Amount	$250,000	$225,000
Included FECC Added to Loan	N/A	$3,000
Included FECC Paid Outside of Closing	N/A	$436.49 (appraisal and credit report fee)
Monthly PI	$1,266.71	$1,074.18
Loan Type	Fixed	Fixed
Loan Term	30 years	30 years
Interest Rate	4.50%	4.00%

$3,436.49 (fees/expenses/closing costs) ÷ $192.53 (PI reduction) = 18 months (17.85 months rounded up to the nearest month)

Example of an ARM-to-Fixed Recoupment Calculation

	Original Loan	New Loan
Base Loan Amount	$200,000	$173,000
Included FECC Added to Loan	N/A	$3,000
Included FECC Paid Outside of Closing	N/A	$436.49
Lender Credit	N/A	$1,000
Monthly PI	$939.55	$851.06
Loan Type	5/1 Hybrid ARM	Fixed
Loan Term	30 years	30 years
Interest Rate	3.00% (initial) 4.00% (current)	4.25%

Calculate the monthly PI for an ARM using the *current* interest rate in place for the ARM. Note that when refinancing an ARM-to-fixed rate mortgage, while the law does not require a reduction in the interest rate, it still requires that the loan be properly seasoned and that all fees be recouped within 36 months of the date of the loan closing. The disclosure standards discussed above also apply.

For the example above, if a lender uses the initial interest rate of 3 percent, the current monthly PI is $843.21. Since the monthly PI for recoupment purposes of the new IRRRL is $851.06, this loan would not meet the recoupment requirement. If, however, the lender uses the current rate of 4.00%, the loan will meet recoupment.

> $3,436.49 (fees/expenses/closing costs) - $1,000.00 (lender credit) = $2,436.49 (net fees/expenses/closing costs) ÷ $88.49 (PI reduction) = 28 months (27.53 months rounded up to the nearest month) <u>Meets 36-month recoupment requirement.</u>

Example of a Fixed-to-ARM Recoupment Calculation

	Original Loan	New Loan
Total Loan Amount	$200,000	$201,000
Included FECC Added to Loan	N/A	$4,000
Included FECC Paid Outside of Closing	N/A	$436.49
Monthly PI	$1,073.64	$847.42
Loan Type	Fixed	5/1 Hybrid ARM
Loan Term	30 years	30 years
Interest Rate	5.00%	3.00% (initial)

Similar to the previous example, the lender must calculate the monthly PI for recoupment using the initial rate on the new IRRRL when the new loan is an ARM.

> $4,436.49 (fees/expenses/closing costs) = $4,436.49 (net fees/expenses/closing costs) ÷ $226.22 (PI reduction) = 20 months (19.61 months rounded up to the nearest month) <u>Meets 36-month recoupment requirement.</u>

Example of a Fixed-to-ARM with Discount Points Recoupment Calculation

	Original Loan	New Loan
Total Loan Amount	$200,000	$203,940
Appraised Value	N/A	$250,000
Included FECC Added to Loan	N/A	$3,000
Included FECC Paid Outside of Closing	N/A	$436.49
Discount Points Added to Loan	N/A	$3,940 (2)
LTV	N/A	82%
Monthly PI	$1,073.64	$859.82
Loan Type	Fixed	5/1 Hybrid ARM
Loan Term	30 years	30 years
Interest Rate	5.00%	3.00% (initial)

In this example, the Veteran is financing 2.00 discount points ($3,940) as part of a Fixed-to-ARM IRRRL and the lower interest rate is solely due to those discount points. As such, the lender must obtain an appraisal and ensure the LTV does not exceed 90 percent. To calculate the LTV, the lender must divide the loan amount by the appraised value ($203,940/$250,000 = 0.82). To calculate the recoupment period, the lender must calculate the monthly PI for recoupment using the initial rate on the new IRRRL when the new loan is an ARM.

> $3,436.49 (fees/expenses/closing costs) + $3,940 (financed discount points) = $7,376.49 (net fees/expenses/closing costs) ÷ $213.82 (PI reduction) = 35 months (34.50 months rounded up to the nearest month) Meets 36-month recoupment requirement.

Example of an ARM-to-ARM Recoupment Calculation

	Original Loan	New Loan
Total Loan Amount	$150,000	$132,000
Included FECC Added to Loan	N/A	$2,000
Included FECC Paid Outside of Closing	N/A	$436.49
Monthly PI	$632.41	$556.52
Loan Type	5/1 Hybrid ARM	5/1 Hybrid ARM
Loan Term	30 years	30 years
Interest Rate	3.00% (current)	3.25% (initial)

> $2,436.49 (fees/expenses/closing costs) ÷ $75.89 (PI reduction) = 33 months (32.11 months rounded up to the nearest month)