

# ***Obama Foreclosure Prevention Plan to Help Resolve Housing Crisis***

Reducing foreclosures is a vital element to success in stabilizing housing markets and prices, and to fostering a recovery in housing and overall economic activity. On February 18, President Obama outlined the multifaceted Homeowner Affordability and Stability Plan (the Plan) that is aimed at preventing millions of foreclosures. The Plan has three main elements: refinance program for borrowers with little equity, but current payments; a \$75 billion loan modification program for struggling homeowners; and, steps to bolster Fannie Mae and Freddie Mac's support to the mortgage market. Details of the mortgage refinance and modification initiatives were released on March 4 as the Making Home Affordable (MHA) program.

## **Homeowner Affordability and Stability Plan**

President Obama unveiled details of a foreclosure prevention plan on February 18, which is designed to help 7 to 9 million responsible homeowners afford their mortgage payments. On March 4, the Treasury Department rolled the loan refinance and modification parts of this plan as the Making Home Affordable program. HASP has three main components, of which the first two are addressed in the MHA program:

- A refinancing program for borrowers who are current on their mortgage payments but who have been unable to refinance because the value of their home has declined.
- A mortgage modification program for borrowers in default, or at imminent risk of default, that builds on the model established by the FDIC by expanding eligibility and establishing incentives for borrowers, mortgage holders and servicers.
- Actions to bolster the financial stability and mortgage support capacity of Fannie Mae and Freddie Mac.

## **Home Affordable Refinance Program**

The refinancing program applies to loans owned or guaranteed by Fannie Mae and Freddie Mac. This program allows borrowers, who because of a decline in their house value, have a mortgage loan-to-value ratio (LTV) of greater than 80 percent, to refinance to a lower interest rate mortgage, even if the new loan would have previously failed to meet Fannie/Freddie requirements.

Fannie and Freddie each released detailed requirements for their respective refinance programs on March 4. Significant features of these programs are:

- Mortgages eligible for refinance must meet Fannie/Freddie eligibility requirements; be seasoned for at least three months; and, the borrower must not have been 30 days or more delinquent in the past 12 months.

- A maximum loan-to-value ratio of 105 percent on the first mortgage and no maximum total LTV, including second liens.
- Relief from standard mortgage insurance requirements for loans with LTV greater than 80 percent. Borrowers who refinance through this program will not be required to obtain additional credit enhancement for a refinanced loan in excess of what already exists for that loan.
- Delivery fees on the refinanced mortgages will be restricted to only the adverse market charge, no other post-settlement delivery fees will be assessed.

The refinancing initiatives will begin on April 1 and the refinanced mortgages must be originated by June 10, 2010. The programs are expected to create mortgage refinancing opportunities for up to 4-5 million homeowners.

### **Home Affordable Modification Program**

This program builds on the loan modification protocol developed by the FDIC, where a loan is modified by reducing the interest rate, increasing the term and/or deferring/reducing principal payments, if such adjustments result in a better net present value for the mortgage investor than disposition through foreclosure. The goal of this program is to reduce homeowners' monthly mortgage payments to sustainable levels. It establishes clear and consistent standards and guidelines for identifying borrowers at risk of default and for loan modifications. It is expected to reach up to 3-4 million at-risk homeowners at a cost of up to \$75 billion (which will be allocated from the Financial Stability Plan/TARP funding). The program is available until December 31, 2012, but loans can only be modified once.

Eligibility is based on high mortgage debt payments compared to income, or borrowers that are underwater. Delinquency is not a requirement for eligibility. This program will also serve homeowners who have not missed payments, but who are in danger of doing so. To increase the potential success rate, the modification program requires HUD-approved counseling for families with high (55 percent) total debt-to-income ratios.

Eligible mortgages must have been originated on or before January 1, 2009. The unpaid principal balance must be equal to or less than \$729,750 (the current loan limit ceiling) and there is no maximum or minimum LTV requirement. The current mortgage payment (including taxes, insurance and homeowner association dues) must be more than 31 percent of the borrower's gross monthly income. Borrowers must have experienced a significant change in income or expenses to the point that current mortgage payment is no longer affordable.

Under the program, a servicer/mortgage holder will first reduce interest payments to achieve a 38 percent mortgage debt-to-income (DTI) ratio. To reach affordability, a homeowners' interest rate may be reduced to as low as 2 percent. If at that rate the debt-to-income ratio still exceeds 31 percent, the lender may extend the term or amortization period to 40 years. The program uses Financial Stability Plan (i.e. TARP) funds to match, dollar-for-dollar, further reductions in mortgage interest payments down to a 31 percent

DTI ratio. If the debt-to-income ratio still exceeds 31 percent, the lender can forbear the principal until the 31 percent target is reached. FSP/TARP funds will be used to subsidize principal reductions.

Modified loan payments will remain stable for at least 5 years, after which payments may be increased by 1 percent per year until the interest rate equals the average interest rate for conforming loans at the time of modification. Borrowers who make timely loan payments will receive a \$1,000 reduction in the principal loan balance each year for up to five years.

Loan servicers will receive FSP/TARP funds for undertaking modifications, for subsequent modification successes, and are offered, along with mortgage holders, additional financial incentives to modify loans prior to default. The program also includes incentives for extinguishing second liens on modified loans. All future recipients of FSP/TARP funds will be required to participate in the loan modification plan.

This program also provides a partial guarantee to mortgage holders (through a \$10 billion insurance fund established by Treasury and FDIC) to offset future declines in the value of the home collateral.

To establish additional motivation for loan modifications, one focus of the program will be to seek legislation to make changes in personal bankruptcy statute that will allow judges to modify mortgage terms, including reductions (cramdowns) of principal obligations. Judicial modifications will apply only to loans under the GSE loan limits. Borrowers seeking a judicial modification must first request a modification from their servicer/lender and certify that they have complied with servicer requests for information. Legislation will also be sought to provide FHA and VA the authority to provide partial claims in the event of a voluntary or judicial modification.

The program will also ease restrictions on FHA's [Hope for Homeowners](#) program, which has thus far resulted in only a few hundred loan modifications. Changes will include reduced fees, increased flexibility for lenders to modify loans, higher debt to income ratios and payments to servicers of existing loans.

Additionally, as part of the stimulus/recovery plan, \$2 billion in Neighborhood Stabilization Program grants will be awarded for innovative programs that reduce foreclosures and an additional \$1.5 billion will to provide renter assistance.

### **Initiatives to Bolster Fannie Mae and Freddie Mac**

HASP also includes several initiatives to bolster the financial stability and mortgage support capacity of Fannie Mae and Freddie Mac. The Treasury will increase its funding commitment to the GSEs by an additional \$100 billion each under the Senior Preferred Stock Purchase Agreements to ensure the strength and security of the mortgage market and to help maintain mortgage affordability. The Agreements were executed as a result of the Fannie/Freddie conservatorship action on September 7 and are indefinite in term. The

\$200 billion in additional GSE funding commitments are being made under the Housing and Economic Recovery Act and do not utilize any funds allocated for the Financial Stability Plan or TARP.

To promote stability and liquidity, the Treasury and the Fed will continue to purchase Fannie Mae and Freddie Mac MBS and debt (up to as much as \$600 billion). Further, to ensure that the GSEs can continue to address problems in the housing finance market, the size of each of the GSEs' retained portfolios allowed under the Senior Preferred Stock Agreements will be increased by \$50 billion to \$900 billion. This will allow the GSEs to continue to support the mortgage markets by freeing up more room under the portfolio cap to acquire mortgages and MBS. Finally, the administration will work with the GSEs to provide support to state housing finance agencies in serving homebuyers.

### **Legislative Developments**

Legislation to implement the statutory changes required by HASP is presently under consideration in the House. On the financial services side, H.R. 1106 includes several pieces of legislation passed by the full House Financial Services Committee in early February, including:

- An overhaul of the Hope for Homeowners mortgage refinancing program to encourage more lenders to participate by reducing fees and write downs, provide incentives for mortgage servicers to engage in modifications under the Program, and reduce administrative burdens to loan underwriters by making the requirements more consistent with standard FHA practices,
- A safe harbor from liability to mortgage servicers who engage in loan modifications workouts or other loss mitigation.
- A permanent boost to the Federal Deposit Insurance Corporation (FDIC) insurance limits, as well as an increase in its borrowing authority.

In addition to these provisions, H.R. 1106 would provide for judicial modification of mortgages in bankruptcy court. Judges would be able to reduce the value of the loan, extend the terms of the loan, lower the interest rate, delay the effective date of an adjustable rate increase, and make other similar changes to a mortgage in order to save the home from foreclosure. In light of the gravity of the foreclosure crisis which continues to depress home values, NAHB began looking at bankruptcy reform as one possible element to solving the foreclosure crisis, but we believe strongly that any changes to the bankruptcy code must be done in a careful manner that will have a positive impact on the marketplace. Specifically, NAHB believes it must be limited in scope, temporary, and apply only to current mortgages.

The House has included several provisions to limit the scope of the bankruptcy provision in H.R. 1106, such as limiting the measure to existing mortgages, as well as the included changes intended to ensure the bill does not negatively impact FHA and VA-backed mortgages. It also would deny relief to individuals who can afford to repay their mortgages without judicial modification and allow lenders to recapture losses if the home

is later sold at a profit. Finally, the bill discourages bankruptcy judges from reducing the value of a mortgage if lowering the interest rate alone would result in affordable payments.

NAHB believes that the bankruptcy provisions in H.R. 1106 must be further narrowed in order to focus only on those mortgages responsible for the surge in defaults. The bill would be improved by adopting several of the principles recently outlined by the Obama Administration. In particular, NAHB is encouraging the House to limit the bankruptcy provisions to mortgages issued in the past few years, as proposed by the Obama Administration. NAHB also supports the Administration's proposal to limit the provision to mortgages below Fannie Mae and Freddie Mac conforming loan limits. This will protect the more volatile jumbo mortgage market, where current rates are already higher than the conforming market, and will further ensure that relief in this bill is targeted to the working families who most need it.

H.R. 1106 is expected to pass the House soon. Additional changes to narrow the bankruptcy provision further are likely in the Senate.