



**Statement of John A. Courson
Chief Operating Officer
Mortgage Bankers Association**

**for the Record of the
House Financial Services Committee**

Hearing on

**“The Implementation of the Hope for Homeowners
Program and A Review of Foreclosure Mitigation Efforts”**

September 17, 2008

Chairman Frank and Ranking Member Bachus thank you for the opportunity to submit this statement for the record regarding the new Hope for Homeowners (HFH) program.¹ The Mortgage Bankers Association² believes the HFH program can become another effective tool for servicers and investors to help keep distressed homeowners in their homes.

The HFH program was created this past summer by the Homeownership and Economic Recovery Act of 2008 (HERA). HERA is an enormous accomplishment for Congress and the housing industry alike. The Act includes several reforms that will help stabilize the market and provide new opportunities for consumers, even as the market continues to evolve in response to great pressures.

Among HERA's important reforms is the HFH program. The HFH was designed as a "rescue plan" to help distressed mortgage borrowers for whom the value of their property has declined below the outstanding amount of their mortgage loan. The Federal Housing Administration (FHA) was given an additional \$300 billion in FHA mortgage insurance authority for the purpose of refinancing eligible borrowers into new, affordable FHA-insured loans with lower fixed rates based on the current property values. These loans would also be made available for securitization through Ginnie Mae.

MBA is working closely with the Department of Housing and Urban Development (HUD), the Department of the Treasury, the Federal Reserve Board and the Federal Deposit Insurance Corporation (FDIC) (collectively known as the Oversight Board) to garner significant support for the HFH program from all constituents, including borrowers, originators, servicers, investors and insurers. MBA has already submitted many comments and suggestions on how to implement the program.

Implementation of Hope for Homeowners

HERA requires that mortgages eligible for refinancing through HFH satisfy three main criteria: 1) the loan was originated on or before January 1, 2008; 2) the borrower's debt-to-income ratio is greater than 31 percent (or a higher ratio set by the Oversight Board) as of March 1, 2008; and 3) the eligible borrower have only one primary residence.

As the Committee is aware, several critical details of the borrower eligibility provisions are still being discussed by the Oversight Board, including underwriting criteria and the formula for equity and appreciation sharing. Until these parameters have been established, the industry cannot accurately identify which borrowers may qualify for the program and, therefore, which borrowers should be considered for pre-implementation forbearance. That said, our members

¹ Sections 1401-1404 of P.L. 110-289 (July 30, 2008).

² The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 370,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

believe that their ongoing forbearance activities likely will capture potential candidates for HFH refinance transactions, although it is likely that many borrowers who are granted forbearance by our members may not ultimately qualify for the HFH program.

As HOPE NOW's Project Lifeline demonstrates, servicers commonly grant forbearance while evaluating a borrower's request for loan modification or other accommodations. Servicers are now performing record volumes of loan modifications and other accommodations to the benefit of millions of borrowers. HOPE NOW data indicate that servicers prevented over 2 million foreclosures through modifications and repayment plans from July 2007 to July 2008. Other modification options are also offered that are not captured in these numbers, including forbearances, advance claims and delinquent refinances.

These activities will continue during the regulation-writing period with the same urgency. Servicers will continue to evaluate borrowers for loss mitigation, including forbearance, modifications, repayment plans and other foreclosure avoidance options. Borrowers with a willingness to retain their home and with reasonable financial means to do so will be considered for a range of options, including forbearance from foreclosure. In many cases, borrowers will be more immediately served through a modification and will not need to wait for the new HFH program.

MBA is also working to make the HFH program the most effective and beneficial tool it can be by sharing its views with the Oversight Board on how to address several critical questions that will ultimately determine how broadly the program can be used. These questions include how to structure the shared appreciation, how to secure the rights to equity and appreciation sharing and what the underwriting standards will be. At the same time, investors, such as Fannie Mae, Freddie Mac and even Ginnie Mae must define the extent to which the program can be used on their pooled or insured loans. MBA has identified several statutory provisions which may limit the applicability of the program and, as they are identified, we are working quickly and closely with the appropriate agencies to develop solutions. Indeed, loan modification and other accommodation activities will continue with the same urgency, even while regulations and guidance are in flux.

Ultimately, the goal is to help more distressed borrowers stay in their own homes. Accordingly, while we work to make HFH the best program it can be, MBA and its members continue to focus on enhancing additional tools, particularly FHASecure, to ensure that borrowers and lenders have a full palette of options available to reach the best possible outcomes.

Principal Reductions

While there is much to admire about the HFH program, we want to emphasize that it is one of many tools available to the industry to help distressed borrowers. In particular, the HFH's core feature of reducing the necessary principal to make borrowers eligible for HFH likely will make producing such loans difficult. Servicers have indicated that they are willing to consider writing down principal to aid distressed borrowers provided that it is not prohibited by the servicing agreements. Principal write-downs are not the only potential aid to borrowers that servicers will consider, however. In evaluating possible courses of action, including principal write-downs, loan modifications and other accommodation options, the servicer generally is legally obligated to seek to minimize investor losses. Based on guidance from the American Securitization Forum, servicers generally have determined the size of the loss by calculating a net present

value of the alternative to the investor (looking at securitization trusts as a whole and not looking at how the modified payment stream would affect different classes of investors in the trust). As the Committee is aware, this guidance was essentially adopted both by Section 1403 of HERA and by California's SB 1137.

As stated at the Committee's hearing on July 25, modifications of the term, interest rate and/or principal deferrals are always preferred over principal write-down as they have less financial impact on the investor and are often more beneficial to the borrower. In the vast majority of cases, affordability can be achieved through modification without the need for principal write-downs.

Moreover, in many cases, modifications and other accommodation options will have less negative impact on the borrower by avoiding premium charges, closing costs and equity/appreciation sharing. As a result, we anticipate that such options will outpace originations of HFH loans. This is not an undesirable outcome – as members of the Committee acknowledged at the July 25 hearing. The objective of HFH and other foreclosure prevention efforts is to keep willing borrowers in their homes when they have reasonable resources to do so. The HFH program will be a valuable tool, but it will have the most value for people for whom other forms of loss mitigation do not work.

Obstacles to Greatest Use of the Program

MBA has been working closely with the Oversight Board to evaluate the various provision of the HFH program and have identified several areas of concern that may reduce borrower or lien holder interest and capacity to participate in the program. We believe the Committee may benefit from a brief discussion of some of these key issues.

* **Market Rates for the Product:** A significant obstacle to originating high volumes of HFH loans is the treatment of these loans in securitization. We understand that HFH loans will not be eligible for the Ginnie Mae TBA market. Instead, HFH loans will be subject to custom pooling, which currently trade at a spread behind Ginnie Mae TBAs, resulting in higher interest rates to borrowers. In some cases, borrowers refinancing into this program will see their interest rates increase. If servicers are required to further reduce principal beyond the 10 percent amount to account for the high cost of the financing, servicers are likely to find loan modification or other alternatives more attractive on a net present value basis. Additionally, it seems likely that borrowers will find the equity and appreciation share provisions less attractive than loan modification and other options.

* **Lien Holder Write Downs:** HERA grants authority to FHA to share future house appreciation with subordinate lien holders. However, the bill appears to exclude first lien holders from recouping any write downs through this same offset. As a result, the program makes it more difficult economically for first lien holders to participate. MBA would welcome a legislative correction of this issue.

* **Possible Treatment as High Cost Loans Under HOEPA:** A critical concern to new originators of HFH loans is the possibility that such loans will exceed the thresholds in the Home Ownership and Equity Protection Act (HOEPA) and therefore become subject to significantly increased liability, including broader rescission, mortgage cancellation penalties and assignee liability. As you know, because of the heightened liability risk of HOEPA loans, lenders simply

do not originate them. At this time, it is unclear how the “appreciation share” must be accounted for in Truth in Lending disclosures and whether the “appreciation share” in itself will contribute to a loan exceeding the HOEPA thresholds where it would not have done so otherwise. Until this issue is resolved, there may be significant reluctance in the industry to originate HFH loans.

* **Fully Insured Loans:** It appears that FHA-insured loans will be eligible for the HFH program. However, it is unclear whether FHA will pay the full claim based on the principal balance (plus other reimbursable amounts) prior to the write down. Unless FHA will provide a full claim, it seems unlikely that servicers will be able to justify the HFH refinance to investors because the transaction would result in the loss of a significant portion of the FHA insurance protection as a result. This loss of coverage likely would make the HFH program fail the net present value test when compared to loan modifications and other options that do not reduce the existing FHA insurance coverage.

* **Representations and Warranties:** HERA requires that originators of HFH loans make certain representations and warranties. Lenders who breach the representations and warranties cannot be paid a claim. In addition, the Act denies insurance on loans where there is a first payment default. These are substantial changes from existing practices, and it seems likely that many lenders will view these changes as significant deterrents to making HFH loans. Depending on how stringently a first payment default is defined, lenders and servicers may not be able to absorb the elevated credit risk associated with making loans to delinquent borrowers.

* **Appraisal Standards:** MBA has significant concerns about the appraisal standards for originating HFH loans. The Act requires the use of certified appraisers, a higher standard than for other FHA loans. While it is critical that the integrity of the valuation process be ensured, there may not be sufficient numbers of certified appraisers in all geographic areas. Delays in closing loans, therefore, may occur unless a long phase-in period is provided. Given that it can take a seasoned appraiser over eighteen months to complete the prerequisites to certification, an appropriately-timed phase-in period is warranted.

In addition, the Act prohibits interested parties from compensating, instructing, inducing, intimidating, not-paying, and reporting in regards to the appraisal. These terms are not terms of art in either the mortgage industry or the legal provision and are interpreted differently in various jurisdictions. It is not difficult to envision numerous scenarios where appraisers and lenders and servicers may have to communicate to resolve conflicts over differences in valuations. If such conflicts cannot be resolved efficiently and effectively, the closing of loans where there are disagreements about valuation may be inhibited. To avoid such a negative result, it is critical that such conversations not be prohibited universally. MBA would welcome legislative correction of the appraisal issues.

FHASecure

As MBA mentioned above, the HFH program is but one of the options available to the industry in working with distressed borrowers. An important alternative to HFH is the FHASecure program. In many ways, FHASecure is more flexible—and, therefore, may be more attractive to both borrowers and industry—than the HFH program. For example, FHASecure allows lien holders to bifurcate mortgages, allows first lien holders to participate, and provides important controls through the recording of two liens. This flexibility, which provides significant benefits to borrowers, more than justifies its continued existence during this time of elevated delinquencies.

While the HFH program is an important option to borrowers and the industry, MBA believes FHASecure is an essential alternative and MBA has strongly urged HUD to keep this program active.

MBA understands that FHA has the authority to make changes to FHASecure's underwriting criteria to allow more distressed borrowers to qualify. MBA would support the following changes and encourages the Commissioner to consider these expansions of the program:

- **Permit delinquent fixed-rate loans to be eligible** – Currently, FHA allows delinquent borrowers with adjustable-rate loans to refinance into *FHASecure* mortgages under certain conditions. Delinquent borrowers with fixed-rate mortgages are not currently eligible. Nonetheless, many borrowers with conventional fixed-rate products have experienced financial hardships for the same extenuating circumstances as ARM borrowers. We recommend that *FHASecure* be expanded to allow the refinance of delinquent conventional fixed-rate loans with extenuating circumstances.
- **Allow delinquencies prior to reset and for reasons other than a rate reset on Interest Only and Payment Option mortgages** – While interest rate changes are one factor affecting delinquency and foreclosure rates, other factors are also impacting these figures. Many borrowers are experiencing financial hardships for reasons other than rate resets. As a result, we recommend that FHA eliminate the requirement that borrowers be current six months prior to rate reset on Payment Option mortgages and Interest Only mortgages. Instead, we recommend that borrowers demonstrate that their delinquencies were due to extenuating circumstances and that they are now capable of affording the new *FHASecure* loan. Similarly, we recommend that FHA eliminate the requirement that lenders demonstrate that a delinquency post-reset was due to an interest rate change, as it is extremely hard for an originator to document. In many cases, the borrower does not become immediately delinquent, but relies for some period of time on savings or investments, making it hard to clearly evidence the reason for default.
- **Reducing the risk of late endorsements** – Lenders must have assurances that FHA will not change its late endorsement policy to require a six-month good payment history. Such a requirement would increase the credit risk to the servicer and reduce the effectiveness of the program.
- **Increase the debt-to-income (DTI) ratio and permit 40-year amortization** – In an effort to help more distressed borrowers, we recommend raising the published DTI threshold and permitting 40-year amortization mortgages. We would welcome further discussions on this issue.
- **Create appropriate compensating factors** – Current borrowers and certain delinquent borrowers are eligible for *FHASecure* even if their DTIs exceed 31/43 percent, provided, however, that there are compensating factors. Those factors are designed for purchase money transactions and not for delinquent refinances. MBA urges FHA to publish compensating factors that more appropriately deal with the *FHASecure* product. MBA is exploring alternatives and will provide recommendations in the near future. In addition, we urge FHA to consider appropriate compensating factors for borrowers that are 90-

days delinquent. Currently, this category of borrower is not eligible to exceed the DTI ratios for any reason.

- **Pool certain refinances with simultaneously created seconds into Ginnie Mae I and II** - Today, a current borrower can refinance his or her first lien mortgage into an FHA-insured loan even when there is a preexisting second that is “underwater.” These loans are eligible for pooling into Ginnie Mae I and Ginnie Mae II. However, a current borrower who refinances a loan into an *FHASecure* mortgage with a simultaneously created “underwater” second must be pooled into a multiple issuer specified Ginnie Mae II MFS pool. Price is significantly worse on these securities, resulting in higher interest rates to borrowers. Assuming no other material underwriting distinction, borrowers in both scenarios are similarly situated from a credit risk perspective. As a result, we request that Ginnie Mae consider pooling *FHASecure* loans made to current borrowers with newly created seconds into Ginnie Mae I and Ginnie Mae II.
- **Allow more severe delinquencies** – Currently, borrowers who are more than 90-days delinquent are not eligible for *FHASecure* even if the new monthly payment under the *FHASecure* loan would make the loan affordable and resolve the delinquency. We request that FHA consider allowing more severe delinquencies to be eligible for *FHASecure*.

Evaluating Servicers on Entire Spectrum of Assistance

Because the HFH program is one of many options available to industry for working with distressed borrowers, the success of foreclosure avoidance efforts cannot be evaluated by focusing solely on the use of the HFH program. While MBA hopes that the HFH program will provide meaningful benefits to many distressed borrowers, as discussed above, many borrowers and industry participants may favor other alternatives, including loan modification. Indeed, as other alternatives of foreclosure avoidance improve, it seems likely that these other alternatives may be even more attractive relative to the HFH program. MBA believes the ultimate goal must be keeping distressed borrowers in their homes, not the implementation of a particular program. MBA, therefore, urges that the industry’s success in working with borrowers be measured in terms of foreclosures avoided, not solely in terms of the volume of HFH loans.

Conclusion

On behalf of MBA, I would like to thank the Committee for the opportunity to present our views on the HFH program and helping distressed borrowers through FHA. While much of the regulatory guidance is still forthcoming, the mortgage industry has already begun to prepare borrowers for the new option the HFH program affords.

MBA looks forward to continuing to work with FHA, the Oversight Board, and this Committee in the future to bring more solutions home to more distressed homeowners.