



Loss Mitigation

Preserving Profitability During Troubled Times

Current Environment

- Record Numbers of Mortgage Defaults (And it's not the economy)
- Investor/Lender Profits Tumble (The Risk was always Greater than Predicted)
 - Investment banks given first-time access to discount window for liquidity
 - National and Regional lenders affected with huge mortgage write-downs
 - GSE's announce losses and dividend cuts
- Regulatory Activism (The Consumer Speaks Up)
 - HOPE NOW
 - Housing and Economic Recovery Act (Foreclosure Prevention)
- Lenders Exit (Is there anyone out there?)
- Servicers (Fixing the Problem is Easier Said Than Done)



Definitions, Concepts and Scope

- Loss Mitigation is meeting your customer's needs at the lowest internal cost.

Concepts

- Customers (External - Consumer, Investor, GSE, Shareholder)
- Customers (Internal – Downstream, Upstream)
- Stakeholders (Regulators, Communities)
- Net Present Value (Maximizing the financial contribution to the (pool, security, ROA etc)
- Identifying and resolving conflicting needs.

Scope of Presentation –

- Measurement of Execution
- Delivery
- Compliance (Investor and Regulatory)
- Fraud (Internal/External)



Default Management and Loss Mitigation

Lauren Bowden
Servicing Quality Control Manager
SunTrust Mortgage



Default Management

- Early Intervention is key-ensure Collections is bringing a delinquent loan current in as short a time possible –test for timeliness of early invention and reviews
- Collections as well as Loss Mitigation should be determining borrower’s attitude and intention towards the debt-be sure files are documented and the account has been fully analyzed to determine reason for default and best course of action
- Ensure correct mailing address and phone numbers are verified
- Determine that verbal financials have been requested –this will determine upfront if a borrower can retain their home and the best path to take
- Collectors and Negotiators should seek commitments from borrowers to cure the delinquency by a specific date-ensure system is noted and proper follow up performed on promises to pay
- Determine Root Cause Analysis for the delinquency and that the best work out option has been developed
- Ensure every opportunity to cure default was presented to borrower if they have not demonstrated a history of broken agreements

Default Management (cont'd)

- Ensure fairness and consistency of reviews
- Ensure there are multiple impact dialing campaigns to mitigate loss and create a pipeline flow into Loss Mitigation
- Test for transitional pipeline between Collections and Loss Mitigation with multiple contact points
- Ensure separate collection procedures on High Risk loans-special teams to manage loans by principal balance and risk with direct feedback to management
- Ensure timely and proper Default Reporting if applicable to minimize interest curtailments
- Ensure proper reporting to consumer reporting agencies
- Determine inspections for delinquent loans are timely and appropriate
- Report to management monthly

Default Management (cont'd)

- First Payment Defaults-embrace a “All Hands on Deck” Philosophy
- Set aggressive initiatives to identify Early Payment Defaults to reduce further potential risk
- Ensure Collections set repayment plans up to six months; beyond that see referral to Loss Mitigation
- Review each loan on a case-by-case basis to see if repay plan is feasible or if Loss Mitigation is appropriate. Repayment plans should be considered first. If on plan-ensure reviewed monthly and that appropriate action is taken if borrower or Servicer failed to comply with terms of agreement
- Service Members Relief Act-to protect members of the military from economic disadvantage when called to service. Ensure proper letters are generated by the 45th day of delinquency and that Orders and letter requesting relief are present if applicable
- Vacant Property-ensure insurance company notified; Collection-Vacant letter sent; determine if property being maintained; ongoing monthly inspections; Realtor contacted; initial securing and winterization performed and property preservation if applicable. If determined property has sustained major damage, ensure insurance department has filed a loss claim immediately. Vacant properties are causing challenges in evolving volatile housing market. There has been a increased effort nationwide to implement vacant property registration ordinances.

Loss Mitigation

- Today, Loss Mitigation is the new timeline management-keep as many borrowers in their homes as possible. Failure to engage in Loss Mitigation and missing deadlines can cause losses and interest curtailments
- Finding viable Loss Mitigation workout strategies benefits both the borrower and the Lender as Loss Mitigation is more cost effective than foreclosure and can minimize credit losses
- Ensure that every opportunity to remedy a default was considered prior to pursuing foreclosure
- Ensure the various effects of available servicing actions were considered in order to generate the smallest financial loss

Quality Assurance

- Ensure loss mitigation letters are sent timely based on Investor Guidelines or Corporate Standards
- Ensure borrower contributions are encourage towards the delinquency and utilized properly towards the loss mitigation option. Contributions may also be a requirement for the retention option
- Servicer should make independent determination of the financial information. Ensure all loss mitigation's documentation regarding income and debts are noted and supporting documentation is present in file. Ensure financial worksheets are being utilized
- Test for a Prioritization by loans in Loss Mitigation:
 - Loans with Foreclosure Sale Dates
 - Loans in Foreclosure
 - Loans longest in the Queue

Quality Assurance (cont'd)

- Loans should be appropriate days delinquent with respect to loss mitigation option being pursued
- Investor Guidelines and Corporate Standards need to be met with respect to timely actions in the management and completion of all loss mitigation workout options-while goal is to keep borrower in home, you do need to minimize losses
- Ensure staff is judicious in their approach to loss mitigation- i.e. look for unrealistic plans or plans or modifications not supported by income
- Determine property value and property conditions are in line with borrower's equity

Quality Assurance (cont'd)

- Agreements from Junior Lien Holders obtained to subordinate their interest-or get an agreement for what Jr. Lien Holder will be willing to accept if Short Sale involved to reduce losses on the 1st
- Ensure timely and proper Default Reporting if applicable
- Loss Mitigation should be pursued up until Foreclosure Sale-Ensure foreclosure fees and costs are paid before stopping a scheduled foreclosure sale to recoup those fees
- Provide monthly feedback to management on findings, trends and losses determined
- Set up specialized reviews for Short Sales and large net losses if determined
- Perform targeted audits of problem areas or trends
- Ensure data integrity reviews are performed for proper coding of Loss Mitigation to assist Loss Mitigation and fulfillment area with Trouble Debt Restructuring initiatives

Loss Mitigation Types

- Repayment Plans-informal if verbally negotiated and will be current within the month or formal-in writing and executed and no longer than 18 months in duration
- Suspended or “No Pay” Plans-allows borrower not to remit payments to overcome current situation within a certain timeframe-not normally longer than 3 months
- Forbearance Plan-(Short and Long Term) –experienced a loss of income or increase in living expenses but will have sufficient income to resume the debt and correct the delinquency within the duration of the special forbearance plan
- Modification-Capitalized interest and escrows and place delinquent amounts onto balance of loan. Title must be clear or subordinations

***Above options should be supported by sufficient income & owner occupancy

Inspections and Property Preservation

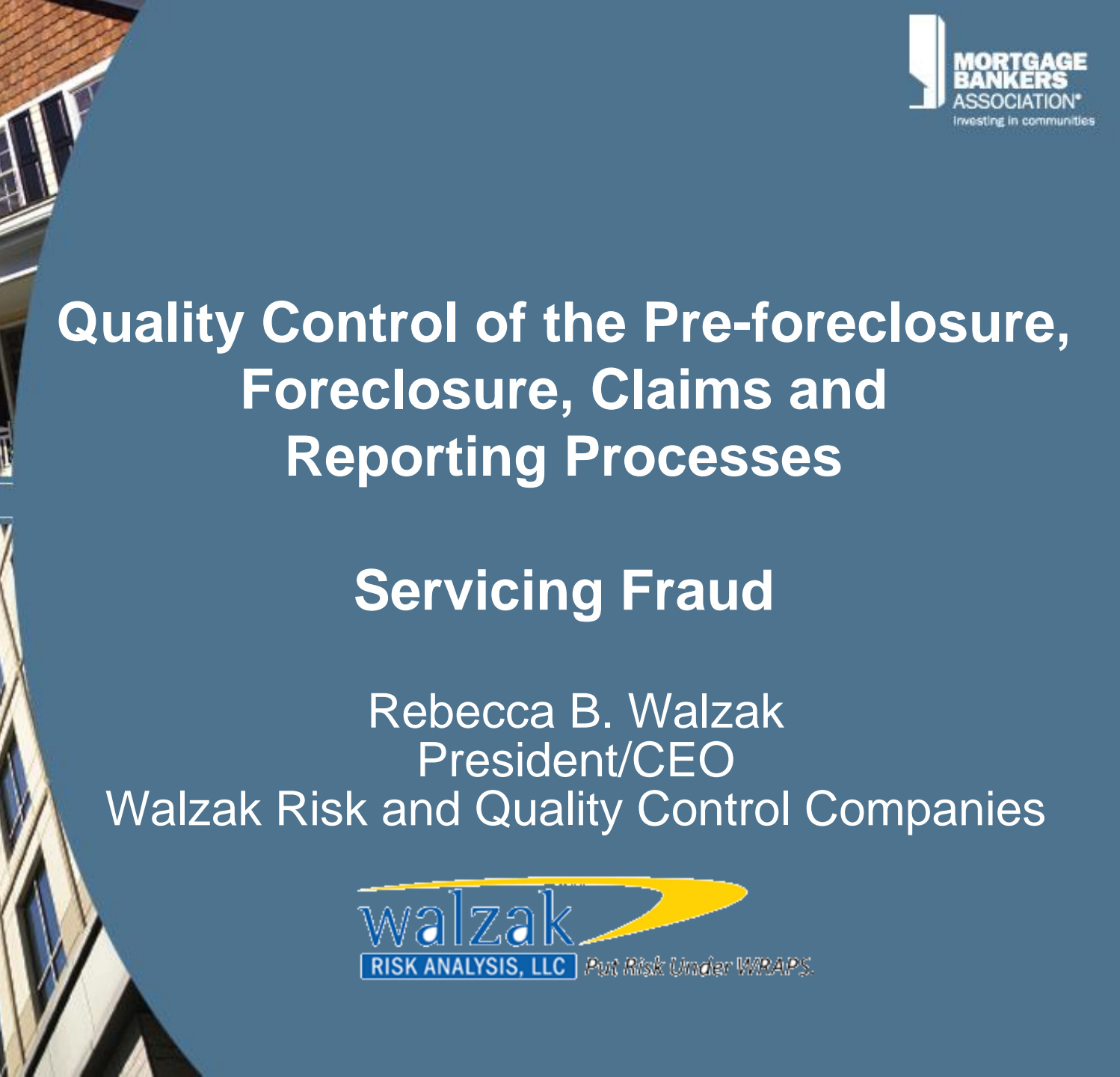
- Ensure all delinquent loans are inspected on Investor/Insurer guidelines-typically every 30 days unless contact made or workout option has been approved-Inspections can be costly
- Consider the less equity a borrower has in their home, the more likely it will become abandoned if in default-abandoned properties must be preserved in order to avoid mortgagee neglect and costs
- Preservation methods should be judged at property inspection-if abandoned or neglected-ensure steps were taken to secure and preserve the property to minimize loss of value
- Inspections should ascertain occupancy and whether tenant or owner occupied. Neglected but occupied properties pose a more difficult risk.
- Ensure if property is noted for sale that Realtor is notified it is their responsibility to preserve and maintain the property
- Vacant or abandoned properties should be inspected every 30 days and contacts to reach borrower should continue
- Damaged property-the property is the sole collateral for the mortgage debt. If the collateral becomes damaged, the home may become unmarketable if it goes to REO and the holder of the note is exposed to a risk of loss
- Have procedures in place for “Bad Addresses” and “Gated Communities” –as Inspectors will still charge for the cost of the inspection in most cases-attempts should be made to contact customer directly to verify occupancy and property conditions and Servicing should have procedures and processes in place

Strategies to Share with business partners in servicing to minimize losses

- Ensure there is focus on available work-out options to avoid foreclosure inclusive of targeted calling and letter campaigns
- Ensure you are seeing frequent contact or call attempts to reach borrower
- Look for proactive approach to contact borrowers while loan in review with Loss Mitigation
- Suggest specific Loss Mitigation calling campaigns designed to contact borrowers based on specific items needed for workout approval
- Detailed analyses of borrower's financial status
- Determine that Loss Mitigation is using forbearance plans in combination with other Loss Mitigation tools
- Utilize various analysis and information tools to identify "At Risk" customers
- Provide ongoing training and feedback exchange
- Ensure your organization has leveraged investor relationships to obtain enhanced delegated authority
- Suggest workout teams are assigned by Investor/Insurer to add increased expertise and knowledge base of workout representatives

Strategies to Share (cont'd)

- Ensure there is a dedicated Loss Mitigation call team to provide efficiency in handling customer inquiry calls
- Develop automated programs to process workouts which will result in increased volumes while ensuring compliance
- Detection of possible fraud in servicing notes or borrower conversations
- Consider Early Stage and Late Stage Collection Teams that request reasons for default, takes interviews and financials and send Loss Mitigation Solicitation packages
- Ensure where possible staff is trained in both Foreclosure and Loss Mitigation timelines and screen at every opportunity for loss mitigation opportunities
- Hone in on Loss Mitigation 2nd review of Denials to look for possible additional loss mitigation opportunities
- Advocate Housing Counseling agencies to assist borrowers during their delinquency-if received early, counseling will aid to bring borrowers current in a shorter period of time
- Participation in groups such as HOPE Now- HOPE now announced for the 2nd quarter 2008 that Mortgage Servicers completed more than 522,000 workouts-up 8% from last quarter



Quality Control of the Pre-foreclosure, Foreclosure, Claims and Reporting Processes

Servicing Fraud

Rebecca B. Walzak
President/CEO

Walzak Risk and Quality Control Companies



Pre-foreclosure Options

- Partial Claim-advance of funds to borrower in an amount necessary for reinstatement of the loan-places lien on property
- Pre-Foreclosure Sale (Short Sale)-Property is sold for an amount that is less than the total amount owed. Requires Clear Title. Servicers should require that a property be listed for at least 90 days before allowing a borrower to seek a Deed-in-Lieu
- Deed-in-Lieu of Foreclosure-Surrender of property back to Investor without a Payoff. Requires Clear Title . Should not be offered on Lot Loans
- Charge Off-while not a Loss Mitigation Option-it is sometimes more advantageous –cease collection efforts when debt is deemed uncollectible. Submit a recommendation to management for a charge off if you have considered all relief and workout options and foreclosure may result in a higher credit loss then charging off your debt

Pre-foreclosure Options (cont'd)

- Based on corporate and/or investor standards, QA should test to determine if:
 - The necessary actions were conducted prior to any of these options being undertaken.
 - This would include an approvals required by investors.
 - Any automated analysis of property value
 - An evaluation of the likelihood of reversing the default.
 - What activities are included in the policies and procedures that involve these actions.
 - What tells you if the activities were conducted or conducted correctly?
 - Is there a specific data field or must you review the files or system notes?
 - What risk is accrued to the servicer if any of these activities are missed or conducted improperly.
 - The greater the likelihood of increased risk, the more critical the activity.

Foreclosures

- **The final alternative** – QA must identify and validate completion of the specific activities involved with this process.
- **Delineate areas of responsibility**
 - Are the responsibilities divided between units or does one unit handle everything?
 - What is the foreclosure process within the organization?
 - Are some functions outsourced to vendors?
If so, how are they managed?
- **Document specific activity responsibilities**
 - Are acceptable fees being charged?
 - Is the staff aware of what is acceptable?
- **Discern what functions are performed by the technology vs. people**
 - Are there activities that are performed by technology?
 - How frequently does that need to be tested?
- **Vendor responsibilities are a critical risk factor with foreclosures.**
 - Are acceptable attorneys used?
 - Are they meeting the standards required by the company?
 - Are they meeting appropriate deadlines?

Claims and Reporting

- **Who is impacted by these areas?**
 - Investors want to know what is going on.
 - Loan status is critical to them for an expected loss and loss reserves perspective.
- **What are the risks?**
 - Depending on the contractual obligation financial losses could be significant to catastrophic.
 - Regulatory reviews, removal of loans from servicing.
 - FHA treble damages.
- **What processes are involved?**
 - Reporting on loan status.
 - Claims for PMI and MIP
- **What activities are involved in these processes?**
 - Validating information
 - Completing required documentation
 - Timeliness of action taken.
- **What tells you they have or have not been completed as required?**
 - What information can you get from system?
 - Is everyone completing activities as required?

Reporting to Management

- **Reports should focus on reliability of the process, not on individual loan files.**
 - Ex. Short sale process activities were ignored on 75% of the files reviewed which resulted in 100% of these files going on to foreclosure.
- **Information on overall process reliability should be statistically valid.**
 - What percentage of the population do the numbers above represent?
 - If I have a biased sample the results are not valid and may result in management taking the wrong action.
- **Areas of weakness should be researched to identify root causes.**
 - Using the example above, conduct a pareto analysis to determine the drivers of these process failures.
 - If it is localized based on a given factor the action to take will be different that if there were no common elements involved.
- **Activity failures should be risk ranked to show relationship to financial, regulatory or reputation risk.**
 - Management should identify what failures cause the most concern to them which will dictate the risk ranking of the findings.

Fraud – The Move to Servicing

- **Fraud is no longer an origination issue.**
 - Previously fraud was thought to be an origination problem.
 - As foreclosures grow, servicing fraud scams grow as well.
 - In addition to the impact on servicing of the origination scams
- **Servicing fraud scams**
 - Most common is “Foreclosure bailout”
 - Equity skimming
 - Identify theft
- **Rollover origination scams**
 - Occupancy issues
 - Straw buyers
 - Property flips
- **Identification process**
 - Training
 - Central reporting and investigations
 - Investor requirements

Conclusion

- Quality Assurance is no longer an “audit”. It is a process analysis that is designed to effectively assist in managing operational risks inherent in the function.
- This paradigm shift has escalated dramatically due to the collapse of the mortgage lending industry and the congressional action.
- There are conceptual frameworks, tools and knowledge available to assist you in the restructuring of your analysis. Take advantage of them.
 - Become familiar with the ASQ
- The MBA Servicing Task Force has designed a new protocol for Servicing QA. It will be available at the Servicing Round Table



Contractual, Regulatory and Legal Requirements for Loss Mitigation

A. Michelle Canter, Esq.
Franzén and Salzano, PC



Requirements for Loss Mitigation

- Contractual ↑↓
- Regulatory ↔
- Legal ↑→↓ ←



Contractual Requirements

- Duty to Investors (investor expectations are high)
- Duty to FHA/VA (programs are changing)
- Duty to shareholders
- Duty to borrowers

Contractual Requirements (Fraud)

- Duty to Investors
 - Report discovery of fraud
 - Triggers buyback / risks relationship
- Duty to Report to FHA/VA (Handbook 4060.1 REV 2, Paragraph 7-3(J))
- Duty to Report to state regulators
 - Report termination of EE for fraud?
 - Report discovery of fraud?

Regulatory Requirements

- Regulators face increasing pressure from state leadership and legislators, as well as consumers
- Critical to monitor evolving state laws and regulations
- Critical to evaluate best practices and not necessarily err on meeting minimum “legal requirements”

Regulatory Requirements (cont'd)

- Additional Notices to Borrowers
 - Prior to Default
 - At time of Default
 - Prior to Foreclosure
- Specific Contact Persons for Lender, Servicer, Designated Loss Mit Agent
- Reports to Regulators of Loss Mit activities

Regulatory Requirements

Illustrative example:

- Maryland Notice of Intent to Foreclose



Legal Requirements – Program Level

- Consumer lawyers itching for next class action lawsuit
- Ensure Loss Mit policies do not violate Fair Lending laws
- Ensure Loss Mit practices (when implemented) do not violate Fair Lending laws

Legal Requirements – Loan Level

- Ensure compliance with TILA and Reg Z
- Ensure compliance with ECOA and FCRA
- Ensure compliance with Fair Debt Collection Practices Act (FDCPA)
- Ensure compliance with state laws

Legal Requirements

Illustrative examples:

- *Pestana litigation (Suffolk Superior Court, Massachusetts)*
- *Other litigation*

Attorneys General lawsuits

- Loss Mitigation practices implicated
 - California
 - San Diego City Attorney joined in
 - Illinois
 - Florida
 - Washington
 - Connecticut (August 2008)
 - Others?

CT Attorney General Suit (Aug 2008)

- When consumers defaulted, the company “bullied them into workouts doomed to fail... crammed unconscionable legal fees into renegotiated loans, digging consumers deeper into debt. The company broke promises that homeowners could refinance, condemning them to hopelessly unaffordable loans.”

CT Attorney General claims:

- Servicers became “insolvency enabler”
- “Stacked the deck and the deal” against its customers
- Predatory lending practices that trap consumers on a “debt treadmill”
- Demanding excessive and inaccurate legal fees in order to reinstate their loans
- Promising suitable payment plans, but demanding loan modifications and repayment plans that were unsustainable, unaffordable or unsuitable.