Making Home Affordable

Update: Foreclosure Alternatives and Home Price Decline Protection Incentives

On Feb.18th the Obama Administration announced the Making Home Affordable (MHA) Program, a comprehensive plan to stabilize the US housing market and offer assistance to up to 7 to 9 million homeowners by reducing mortgage payments to affordable levels and preventing avoidable foreclosures.

As promised, two weeks later on March 4th, the Administration published detailed program guidelines and authorized servicers to begin modifications and refinancings under the plan immediately. On April 28th, the Administration announced additional details related to the Second Lien Program and strengthening Hope for Homeowners. Fourteen servicers, including the five largest, have now signed contracts and begun modifications and refinancings under MHA. Between loans covered by these servicers and loans owned or securitized by Fannie Mae or Freddie Mac, more than 75 percent of all loans in the country are now covered by the MHA program.

Today we are providing a program update, including additional details on Foreclosure Alternatives and Home Price Decline Protection Incentives. Foreclosure Alternatives will help to prevent costly foreclosures by providing incentives for servicers and borrowers to pursue short sales and deeds-in-lieu of foreclosure in cases where a borrower is eligible for a MHA modification but unable to complete the modification process. This program will assist homeowners who cannot afford to stay in their homes by helping them to avoid foreclosure and relocate to a home they can afford. Building on insights developed by the FDIC, Home Price Decline Protection Incentives will provide additional payments based on recent home price declines, and therefore will incentivize additional modifications in areas where home prices have been falling. By increasing MHA modifications and the use of alternatives to foreclosure, we will reduce the negative impact of foreclosure, minimizing damaging costs for financial institutions, borrowers and communities.

Home Price Decline Protection Incentives and Foreclosure Alternatives, together with the other comprehensive elements of the Making Home Affordable program, will help to stabilize property values for homeowners in neighborhoods hardest hit by foreclosures. Based on estimates of the relationship between foreclosures and home prices, the Home Affordable Modification program could help to bolster home values for the average homeowner by as much as $6,000.

Foreclosure Alternatives and Home Price Decline Protection Incentives

1. Foreclosure Alternatives for Borrowers Eligible for MHA

- Short Sales/Deeds-In-Lieu Program to Facilitate Foreclosure Alternatives
  - Incentives for servicers to pursue alternatives to foreclosures
  - Borrower incentives to cover relocation expenses to homes that are affordable
  - Streamlined process combining short sales and deed-in-lieu transactions

2. Home Price Decline Protection Incentives to Protect Against Falling Home Prices

- Incentives to support modifications in markets hardest hit by falling home prices
  - Provides incentives for modifications by providing payments based on recent declines in home prices to reduce the risk of loss to lenders from modifications compared to alternatives that could result in the loss of homeownership

1. **<u>Foreclosure Alternatives for Borrowers Eligible for MHA but Unable to Sustain a Modification</u>**: For eligible borrowers unable to retain their homes through a Home Affordable Modification, MHA will provide incentives to borrowers, servicers and investors to encourage short sales and deeds-in-lieu. Both allow families and servicers to avoid the costly foreclosure process, and to minimize the negative impact of foreclosures on borrowers, financial institutions and communities.

   Short Sales/Deeds-In-Lieu Program to Facilitate Foreclosure Alternatives

   When a borrower meets the eligibility requirements for a Home Affordable Modification (HAMP) but does not qualify for a modification or cannot maintain payments during the trial period or modification, the servicer may consider a short sale, and if that is unsuccessful, a deed-in-lieu (DIL).

   Both a short sale and a DIL provide an opportunity for borrowers and servicers to avoid the foreclosure process. In a short sale, a servicer allows the borrower to sell the property at its current value, even if the sale nets less than the total amount owed on the mortgage. Approval of a short sale requires the borrower to list and actively market the home at its fair value. The sale must be an arms length market transaction with all proceeds (after selling costs) applied to the discounted mortgage payoff. If the borrower actively markets the property but is unable to sell it within the agreed upon time period, a servicer may consider a DIL. With a DIL, the borrower voluntarily transfers ownership of the property to the servicer – provided the title is free and clear.

   Short sales and DILs are complex transactions involving careful coordination and close cooperation among a number of parties -- servicers, appraisers, borrowers, purchasers, real estate brokers, title agencies and often mortgage insurance companies and junior lien holders. A short sale or DIL usually provides a better outcome for borrowers, investors and communities. However, due to the complexity of and time required for completion of these transactions, servicers historically have often opted to pursue foreclosure instead, even where a short sale or DIL would have provided a substantially better outcome for borrowers, investors and communities.

   The MHA Foreclosure Alternatives Program simplifies and streamlines the short sale and DIL process by providing a standard process flow, minimum performance timeframes and standard documentation. To compliment a standardized approach, Treasury provides incentives to borrowers, servicers and investors to pursue short sales and DILs.

   <u>How The Home Affordable Short Sale/DIL Program Works</u>:

   - <u>Borrower Eligibility</u>. Borrowers will be eligible for the Foreclosure Alternative Program if they meet the minimum eligibility criteria for a Home Affordable Modification but did not qualify for a modification or were unable to sustain payments under a trial period plan or a modification. Prior to proceeding to foreclosure, participating servicers must evaluate each eligible borrower to determine if a short sale is appropriate. Considerations in the determination include property condition and value, average marketing time in the community where the property is located, the condition of the title including the presence of junior liens and a determination that the net sales proceeds are expected to exceed the investor's recovery through foreclosure <u>Incentive Payments</u>.

    - Servicers may receive incentive compensation of up to $1,000 for successful completion of a short sale or DIL.
    - Borrowers may receive incentive compensation of up to $1,500 to assist with relocation expenses.
    - Treasury will also share the cost of paying junior lien holders to release their claims, matching $1 for every $2 paid by the investors, up to a total contribution of $1,000 by Treasury.

- Standardized Documentation: The program will publish streamlined and standardized documentation, including a Short Sale Agreement and an Offer Acceptance Letter. These documents will outline specific marketing terms, describe the rights and responsibilities of all parties and establish clear timeframes for performance. Creating one standard set of documents that the industry can use is expected to minimize the complexity of these transactions and significantly increase use of the short sale option.

- Property Valuation: The servicer will independently establish both property value and the minimum acceptable net return in accordance with investor guidance and will provide instruction to the borrower regarding the list price and any permissible price reductions. The price may be determined based on either: (1) an appraisal performed in accordance with USPAP and/or (2) one or more Broker Price Opinions either of which must be dated within 120 days of the Short Sale Agreement.

- Minimum and Maximum Duration: Under the program, servicers will allow borrowers at least 90 days to market and sell the property, with possibly more time based on local market conditions. The property must be listed with a licensed realtor experienced in selling properties in the neighborhood. Marketing of the property may run concurrently with the foreclosure process, however no foreclosure sale can take place during the marketing period specified in the Short Sale Agreement as long as the borrower is acting in good faith to sell the property. There will be a maximum marketing period of 1 year for the property, provided any longer period not otherwise delay foreclosure sale, to ensure diligence by servicers and borrowers in moving as quickly as possible to complete the short sale and deed-in-lieu process.

- Selling Commissions and Fees: Reasonable and customary real estate commissions and selling costs that may be deducted from the sales price will be specified in the Short Sale Agreement. The Servicer will agree not to negotiate a lower sales commission after an offer has been received.

- Fees and Charges: Servicers may not charge borrowers fees for participation in the Foreclosure Alternative Program.

- Property Eligibility: Any junior liens, mortgages or other debts against the property must be cleared for the property to be sold as a short sale or deeded to the servicer. The servicer can proceed with a short sale or deed-in-lieu if there is a reasonable belief that all liens on the property can be cleared.

- Program Expiration: Eligible borrowers will be accepted until December 31, 2012. Program payments will be made upon successful completion of a short sale or DIL.

- Deed-in-Lieu: At the servicer's option, the Short Sale Agreement may include a condition that the borrower agrees to deed the property to the servicer in exchange for a release from the debt if the property does not sell within the time specified in the Agreement or any extension thereof. In this case the borrower would have 30 days to vacate the property and would be entitled to $1,500 to assist with relocation expenses, in addition to any other funds the servicer may provide to the borrower.

2. **Home Price Decline Protection Incentives to Protect Against Falling Home Prices:** This initiative provides lenders additional incentives for modifications where home price declines have been most severe and lenders fear these declines may persist. These incentives will encourage servicers to undertake more modifications by assuring that incremental investor losses will be partially offset.

   To encourage the modification of more mortgages and enable more families to keep their homes, the Administration, building on insights pioneered by Chairman Bair and the FDIC, has developed an innovative payment that provides compensation based on recent home price declines, structured as a simple cash payment on every eligible loan. Home Price Decline Protection (HPDP) incentives are designed to address investor concerns that recent home price declines may persist. Together the incentive payments on all modified homes will help cover the incremental collateral loss on those modifications that do not succeed. HPDP payments will be linked to the rate of recent home price decline in a local housing market, as well as the average cost of a home in that market.

- ***Increases Number of Loans that Are Modified:*** Making Home Affordable will make payments totaling up to $10 billion to to encourage lenders, servicers and investors to modify rather than foreclose by addressing concerns that home price declines will persist in the future. This should increase the number of modifications completed under the MHA program in markets hardest hit by falling home prices.

How The Program Works:

- Payments will be based on the total number of modified loans that successfully complete the modification trial period and remain in the modification program.

- Each successful modification will be eligible for a HPDP incentive, up to a cap for HPDP incentives of $10 billion.

- If the trial modification remains successful, $1/24^{th}$ of the HPDP incentive will accrue to the lender/investor each month for up to 24 months. HPDP incentive payments will be made at the end of the first and second year of the modification.

- Calculation of HPDP Incentives: HPDP incentive amounts will be calculated based on a formula incorporating:

  - Declines in average local market home prices over recent quarters prior to the quarter in which the loan was modified based on housing price indices; and

  - The average price of a home in each particular market, since the potential loss due to a given rate of home price decline will be larger in higher cost areas.