

Current Developments in Foreclosure Prevention



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Title 5 Safe Mortgage Licenses Act

President Bush signed into law the Secure and Fair Enforcement (SAFE) Mortgage Licensing Act on July 30, 2008 as a central part of the Housing and Economic Recovery Act (HERA).

This act sets forth procedures, requirements, education, testing and new standards including mandatory national registration of all depository mortgage loan originators (RMLOs) plus the state licensing of non-depository mortgage loan originators (MLOs), through the creation of a Nationwide Mortgage Licensing System and Registry, known as the NMLS. The SAFE Act is regulated by the Department of Housing and Urban Development (HUD).

Every loan originator taking a residential mortgage loan application from a consumer must obtain a mortgage loan originator license from the State Agency in which the subject property is located. States are required to set certain minimum requirements for obtaining Licenses.

A new loan officer must complete 20 hours of pre-licensing education. The course will usually cost around \$350. States may require one to five additional hours of state-specific training. States may accept past hours taken for this requirement.

Each year, at least eight hours of continuing education are required to maintain licenses. An additional 1 to 5 hours of state-specific education may also be required.

A national standardized test of federal laws and regulations must be passed by each licensee. State-specific components may be added. National tests are \$92 with the state component running \$69. The tests only need be passed once. The national test has 100 questions. State specific tests range between 45-65 questions. Not every state has state specific education, but every state has a state specific test.

Fingerprints are sent to the FBI for a criminal background check of each applicant. Completed reports are sent to the state. Some states may check their local criminal database. No felonies may have occurred in the previous 7 years or ever if financial services related. The federal fingerprinting costs \$39 and the state fingerprinting average \$40.

Each state is required to review a credit report for each licensee. No minimum credit standard has been set at the national level. Credit standards are at this time state specific.

States have a license application fee ranging from \$50 to \$500. It must be completed through the Nationwide Mortgage Licensing System (NMLS).

A privately owned and operated website processes applications. NMLS does not review or approve license applications. The system can process test results, collect fees for federal fingerprinting. It is planned that the system will collect fees for credit reports in all states. It tracks status for, education, tests and fingerprints.

2MP (SECOND LIEN MODIFICATION PROGRAM)

Many homeowners may be struggling to make their monthly mortgage payments because they have a second lien. Even when a first mortgage payment is affordable, the addition of a second lien can sometimes increase monthly payments beyond affordable levels. Second liens often complicate or prevent modification or refinancing of a first mortgage.

The 2nd Lien Modification Program (2MP) offers homeowners a way to lower payments on their second mortgage. 2MP offers homeowners, their mortgage servicers, and investors an incentive for modifying a second lien. Servicers and investors may also receive an incentive for extinguishing a second lien, forgiving all of the debt a homeowner owes.

Homeowners must provide consent to share their first lien mortgage modification information with their second lien mortgage servicer, if they are different. Since 2MP is meant to be complementary to the Home Affordable Modification Program (HAMP), a homeowner must have their first lien modified through HAMP before the second lien can be modified under 2MP.

Under 2MP, with their investor's guidance, a mortgage servicer may:

- Reduce the interest rate to one percent for second liens that pay both principal and interest (amortizing);
- Reduce the interest rate to two percent for interest-only second liens
- Extend the term of the second lien to 40 years
- If the principal was deferred (through forbearance) on the first lien, a servicer must forbear the same proportion on the second lien;
- If the principal was forgiven on the first lien, in accordance with the Principal Reduction Alternative program, a servicer must forgive the same proportion on the second lien; although a servicer may, forgive a portion or the entire second lien and will receive incentives for doing so.

A second lien is eligible for 2MP if:

- the corresponding first lien has been modified under the Obama Administration's Home Affordable Modification Program and the second lien servicer is participating
- it was originated on or before January 1, 2009;
- it does not have an unpaid principal balance (at consideration for the modification) of less than \$5,000 or a pre-modification scheduled monthly payment of less than \$100
- it has not yet been modified under 2MP;
- it is not subordinate to a second lien or is not a home equity loan in first lien position
- it is not a second lien on which no interest is charged and no payments are due until the first lien is paid in full; and
- the second lien servicer is in possession of a fully executed 2MP modification agreement or trial period plan by December 31, 2012 or the second lien is not insured, guaranteed, or held by a Federal government agency (e.g. FHA, HUD, VA, and Rural Development).

Reprinted from http://makinghomeaffordable.gov/lien_modification.html

A brief look at the state of the housing market

Stabilizing the housing market is the key to economic recovery.

Foreclosure activity has increased on a year-over-year basis for 44 consecutive months, and is unlikely to slow down until 2011. Foreclosure activity will probably peak in 2010. REO inventory will remain high until 2013. "Strategic Defaults" will increase (where the family decides to short sale their home, as they are so far upside down). Current loan modification programs will not be effective to stop the trend. Projections indicate 4,500,000 total US foreclosure filings in 2010. The most likely scenario is that these homes will be marketed very slowly over the next 3-4 years so not to have another housing market crash. Overall, we are in for a long, slow recovery.

A significant number of current home sales activities are foreclosures or short sales. Higher priced homes are moving more slowly, and there's still a significant inventory. And it's unclear how many homes in the foreclosure process will eventually be on the market.

The "Making Home Affordable" program was an attempt to stem this trend. However the re-default rate on modified loans is running about 50%. The **Treasury Department** issued a notice to mortgage servicers on Oct. 6, 2010, participating in the Home Affordable Modification Program (HAMP), reminding them of the requirement to exhaust all possible loss mitigation alternatives before foreclosing.

Consumer advocates have also reported examples of homeowners being offered modifications that don't comply with the Home Affordable program and homeowners being denied a modification without clear justification. The process is not transparent. Realty Trac reports that foreclosure actions are still on the rise. Job losses will likely only drive those numbers up—even among well underwritten loans. In the second quarter of 2010, foreclosures for prime mortgages continued to outpace efforts to help families remain in their homes. In addition to the problems in the commercial real estate market, a wave of option adjustable rate mortgages will reset in the next four years. The number

of mortgages in question could be close one million. Already, 10% of payment option ARMS are in the process of foreclosure, three times the 2.9% rate for all mortgages.

Nationally, the number of days from when a borrower stops paying on his/her mortgage to when the bank sends out the first foreclosure notice can be up to 400 and the final foreclosure can take up to a year longer. The government's Home Affordable Modification Program has made little progress in stemming the onslaught of foreclosures and is simply delaying the inevitable.

"Ivy Zelman, CEO of Zelman & Associates, with over 17 years of experience covering housing and housing-related industries did a simple exercise of adding shadow inventory to the seemingly improving inventory numbers. In Washington D.C. for example, she cites a 5.1 month supply of homes for sale, well below the nation's 8 month supply. But add the shadow inventory of foreclosures, and you get a 13.2 month supply. She claims Builders who are "underwriting ground are unaware of these headwinds. On the low end of the market, that is, homes priced below \$150,000, investors comprise 2/3 of the purchasers." Campbell Surveys also found that 50 percent of current sales were of distressed properties (foreclosures or short sales.) "The trouble is the higher end of the market, over \$400,000 where investors can't buy with all cash and the mortgage market is limited." Zelman cites a 45 month supply of homes between \$400-600,000. "The government is ignoring the higher end of the market, and ignoring higher end borrowers who may be in trouble due to unemployment. Jumbo loans are excluded from the federal mortgage bailout" according to Zelman.

Housingwire: states that "Bank of America is considering a special program for unemployed borrowers that would offer as many as nine months of no mortgage payments while they hunt for a new job."

According to Dean Baker, co-director of the Center for Economic and Policy Research, "a very high percentage of the permanent modifications are likely to end in default." The money that the government spends on a failed modification goes to banks, not

homeowners. Additionally, if refinanced rather than modified under the program, the government will have substituted an FHA insured mortgage for the original mortgage issued by a bank. This means that when a re-default takes place, the bank will have received most of the principle back on the loan, with the government incurring the loss on the re-default.”

"The end of the tax credit has clearly had an effect," stated Thomas Popik, research director for Campbell Surveys. "First-time homebuyer participation is continuing to drop. We expect a further decline in first-time homebuyer activity, perhaps reaching as low as 30-35% of the market by the fall months.”

The costs of owning a home can substantially outweigh the benefits because of issues such minimal home equity retention and an owners desire to "flip" a home on the market quickly, researchers Wenli Li and Fang Yang said in their report *American Dream or American Obsession? The Economic Benefits and Costs of Homeownership*, published Fall 2010 by the Federal Reserve Bank of Philadelphia.

"One thing that is certain," the two analysts said, "is that homeownership is not for everyone, and thus, based on economic benefits, the case for trying to achieve a nation of homeowners needs to be rethought."

Many borrowers agree with them, especially ones that have never owned a home before. According to a *Monthly Survey of Real Estate Market Conditions* by Campbell Surveys and *Inside Mortgage Finance*, first-time homebuyer activity is down from its peak of 48.2% in March 2010, to the lowest level seen in the past year now below 39% of the buyer market.

First-time homebuyers are critical to the housing market because they soak up excess existing inventory, including distressed properties that continue to infiltrate the market. The decrease in first-time buyers will likely put more downward pressure on home prices in the coming months. The faltering first-time homebuyer market is likely attributed to the expiration of the tax-credit option in June 2010.

HAFAs (Home Affordability Foreclosure Alternative)

HAFAs is a program for homeowners who cannot qualify for a HAMP modification under the Home Affordable Modification Program (HAMP). With HAFAs homeowners avoid a foreclosure by selling their home under the terms of a “short sale”. This is the sale of a home at or below current market value when that sale nets the seller’s mortgage lender(s) less than the outstanding balance of the subject’s mortgage.

The program uses the borrower’s financial and hardship information already collected under HAMP and allows borrowers to receive preapproved short sales terms in tandem with listing the property for sale. When the transaction is successfully completed a \$3,000 relocation bonuses is paid to the borrower. Junior liens may be retired at 6% of the outstanding principal balance or \$6000.00, whichever is less.

All HAMP participating servicers may implement their own written policy as long as they are consistent with investor guidelines. This policy may include magnitude of potential loss, local market influences, the timing of pending foreclosure actions as well as borrower cooperation. The program ends December 31, 2012.

Servicers must consider HAMP applicants for HAFAs **within 30 calendar days** after the borrower does not qualify for a HAMP, fails to successfully complete a HAMP trial period plan, misses at least two consecutive payments, or requests a short sale or deed-in-lieu. If the short sale is unsuccessful the seller is allowed to transferring title to the lender through a “deed-in-lieu of foreclosure.

If the servicer determines a borrower is eligible for a short sale or deed-in-lieu, the borrower, must notify the borrower in writing of these options and give the borrower 14 calendar days to respond, orally or in writing. If the borrower does not respond the servicer’s duty terminates under the terms of HAFAs. If the borrower asks for a short sale

or deed-in-lieu and does not qualify, the servicer must inform the borrower and provide a toll-free number for follow up communication.

If qualified, a Short Sale Agreement (SSA) is completed and sent to the borrower. The borrower has 14 calendar days, from the issuing date of the SSA, to sign and return. Borrower's real estate broker must also sign the SSA. The SSA must give the borrower an initial period of 120 calendar days to sell the house which may extend up to a total of 12 months, if agreed to by the borrower and servicer. Within 3 business days of receiving an executed sale contract, a completed Request for Approval of Short Sale (RASS) must be returned to the servicer with; a copy of the sale contract, all addenda, all buyer's documentation of funds or mortgage preapproval letter, all information on the status of any and all subordinate liens outstanding. Within 10 business days after the servicer receives the RASS and all required attachments, the servicer must approve or deny the request and advise the borrower with a statement of the reasons in the case of disapproval. The servicer may not require the closing to take place any sooner than 45 calendar days from the date of the sales contract. The servicer must follow local and/or state laws for the timing of the release of its first mortgage lien. If local or state law does not govern, the servicer must release its first mortgage lien within 30 business days. Investors must waive rights to seek deficiency judgments and may not require a promissory note for any deficiency. These rules also apply to junior lien holders receiving incentives.

HAMP (Home Affordability Modification Program)

U.S. Treasury will partner with financial institutions to reduce homeowners' monthly mortgage payments through modification of the existing lien.

The home must be an owner occupied, single family 1-4 unit property, condominium, cooperative, and manufactured home affixed to a foundation and treated as real property under state law and may not be vacant or condemned.

- First lien loans must have an unpaid principal balance (**prior to capitalization of arrearages**) equal to or less than: 1 Unit: \$729,750, 2 Units: \$934,200, 3 Units: \$1,129,250, 4 Units: \$1,403,400
- The borrower must have a financial hardship. This may have been caused by an increase in mortgage payment, personal expenses, divorce, loss of health, death or loss of income.
- Borrowers must warrant that they do not have sufficient liquid assets to make their monthly mortgage payments.
- Borrowers in bankruptcy are not automatically eliminated from consideration for a modification.
- Borrowers in active litigation regarding the mortgage loan can qualify for a modification without waiving their legal rights.
- Any foreclosure action will be temporarily suspended during the trial period, or while borrowers are considered for alternative foreclosure prevention options. **Borrowers in foreclosure restart states will be considered to have failed the Trial Period if they are not current at the time the foreclosure sale is scheduled.**
- New borrowers will be accepted until December 31, 2012.
- There is no minimum or maximum Loan to Value (LTV) ratio for eligibility purposes.
- Consideration for a Hope for Homeowners refinance should not delay eligible borrowers from receiving a modification offer and beginning the Trial Modification Period.

Front-End Ratio is PITIA/Monthly Gross Income. PITIA is defined as principal, interest, taxes, insurance (including homeowners insurance and hazard and flood insurance) and homeowners association and/or condominium fees.

The **borrower's income** will be verified by requiring a signed Form 4506-T (Request for Transcript of Tax Return) and obtaining the most recent tax return on file for each borrower on the note. **For wage earners**, the two most recent pay stubs for each wage earner on the note will also be required. **For self-employed borrowers** or for non-wage income, the borrower's income will be verified by obtaining other third party documents that provide reasonably reliable evidence of income.

Subordinate liens are not included in the Front-End Debt to Income (DTI) calculation, but they are included in the Back-End DTI calculation. Mortgage insurance premiums are excluded from the PITIA calculation.

The Back-End DTI is the ratio of the borrower's total monthly debt payments (such as Front-End PITIA, any mortgage insurance premiums, payments on all installment debts, monthly payments on all junior liens, alimony, car lease payments, aggregate negative net rental income from all investment properties owned, and monthly mortgage payments for second homes) to the borrower's Monthly Gross Income.

The servicer must validate monthly installment, revolving debt and secondary mortgage debt by pulling a credit report for each borrower or a joint report for a married couple. The servicer must also consider information obtained from the borrower orally or in writing concerning incremental monthly obligations.

A standard Net Present Value (NPV) Test will be required on each loan. This NPV Test will compare the Net Present Value (NPV) of cash flows expected from a modification to the net present value of cash flows expected in the absence of

modification. If the NPV of the modification scenario is greater, the NPV result is deemed positive. The NPV Test applies to the Standard Waterfall (the order in which the modification should take place) only and does not require consideration of principal forgiveness. However, **the servicer may choose to forgive principal if the servicer determines that principal forgiveness improves the likelihood of loan performance** and the value of modification.

If the NPV Test generates a positive result, the servicer is required to offer a Home Affordable Modification to the borrower. **If the NPV Test generates a negative result, modification is optional, unless prohibited under contract.** The monthly payment reduction incentive is available for any Home Affordable Modification, whether or not NPV positive, that meets the eligibility requirements and is performed according to the Standard Waterfall described below.

If the NPV Test result is negative and a Home Affordable Modification is not pursued, the lender/investor must seek other foreclosure prevention alternatives, including alternative modification programs, deed-in-lieu and short sale programs.

Servicers will follow the Standard Waterfall described below to reduce monthly payments to the 31% Front-End DTI Target defined above. **The initiative will reimburse lenders/investors for one half of the cost of reducing monthly payments from a level consistent with a 38% Front-End DTI Ratio (or less, if the unmodified DTI is less than 38%) down to a level consistent with a 31% Front-End DTI Ratio. This Payment Reduction Cost Share can last for up to five years.**

Servicers may capitalize accrued interest, past due real estate taxes and insurance premiums, delinquency charges paid to third parties in the ordinary course of servicing and not retained by the servicer, any required escrow advances already paid by the

servicer and any required escrow advances by the servicer that are currently due and will be paid by the servicer during the Trial Period. **Late fees are not capitalized.**

The **note rate should be reduced in increments of 0.125 %**, and should bring the monthly payment as close as possible to the Front-End DTI Target without going below 31%. The floor rate is 2%. **If the resulting modified interest rate is at or above the Interest Rate Cap, this modified interest rate will be the new note rate for the remaining loan term.** If the resulting modified interest rate is below the Interest Rate Cap, this modified interest rate will be in effect for the first five years, followed by annual increases of 1% (100 basis points) per year or such lesser amount as may be needed until the interest rate reaches the Interest Rate Cap, at which time it will be fixed for the remaining loan term.

If the Front-End DTI Target has not been reached at the floor rate of 2%, the term may be extended up to 40 years.

If the Front-End DTI Target has not been reached forbear principal.

If there is a principal forbearance amount, a balloon payment of that forbearance amount is due on the maturity date, upon sale of the property, or upon payoff of the interest bearing balance. If the option to forebear principal is selected, the servicer shall forbear on collecting the deferred portion of the Capitalized Balance until the earliest of (i) the maturity of the modified loan, (ii) a sale of the property, or (iii) a pay-off or refinancing of the loan. Successful completion of the trial modification period and entry into program agreements between the servicer and Treasury's financial agent are prerequisites for any payments to the lender/investor, servicer, or borrower. No interest will accrue on the forbearance amount.

If the modification does not pass the NPV Test and the servicer chooses to modify the loan, the modified balance must be no lower than the current property value. If principal

is forgiven and the rate is not reduced, the rate will be frozen at its existing level and treated as a modified rate for the purposes of the Interest Rate Cap.

In the event of principal forgiveness, the Payment Reduction Cost Share continues to be based on the change in the borrower's monthly payment from 38% to 31% Front-End DTI ratio and is limited to five years.

If the modified rate exceeds the interest rate cap, **The "Interest Rate Cap" is the Freddie Mac Weekly Primary Mortgage Market Survey (PMMS) Rate for 30-year fixed rate conforming loans, rounded to the nearest 0.125 percent, as of the date that the Agreement is prepared**, the modified rate will be the new note rate for the remaining loan term.

Modification is effective the first calendar month following the successful completion of the Trial Period. Successful completion means that the borrower is current at the end of the Trial Period. The Trial Period will last 90 days (three payments at modified terms) or longer if necessary to comply with investor contractual obligations.

Servicers are **required to escrow** for modified borrowers' real estate taxes and mortgage-related insurance payments immediately if they have the capability of processing these payments or are already using a third-party vendor for this purpose.

For borrowers with a Back-End DTI of 55% or higher, the servicer must provide the borrower with a letter stating that counseling is a requirement of the modification terms. This letter may be required by counselors in order to begin counseling. The modification will not take effect until the borrower represents in writing that he or she will obtain counseling.

Unpaid late fees will be waived for the borrower. These include late fees prior to the start of the Trial Period and accrued during the period.

There are no modification fees or charges borne by the borrower.

The investor may not require the borrower to contribute cash.

Borrowers will be eligible to accrue up to \$1,000 each year in Pay-for-Performance Success Payments for up to five years, a total of up to \$5,000 over five years. Accruals are based on on-time payment performance. To qualify for borrower Pay for Performance Success Payments, the modification must reduce the monthly payment by a minimum of 6 %. The monthly payment is the PITIA payment, as used in defining DTI, with the loan fully indexed and fully amortized.

Net Present Value

The program allows the servicer to choose the Discount Rate to use in the NPV Model, subject to a program-determined ceiling that will be sensitive to the market-determined cost of funds. The ceiling on the allowable Discount Rate for the NPV Test is the Freddie Mac Primary Mortgage Market Survey rate (PMMS), plus a spread of 2.5 percentage points. The PMMS is the conventional mortgage rate published in the Federal Reserve's H.15 bulletin.

The servicer may choose a different Discount Rate for loans in portfolio versus loans in investor pools, but may not otherwise apply different rates to different loans in the servicing book. For example, it may choose to use a Discount Rate equal to the PMMS + 2.0 percent for its investor pools and a Discount Rate equal to the PMMS for its loans in portfolio.

For loans that have mortgage insurance (MI) coverage, the NPV Test will incorporate the value of the contingent claim payment in the event of default when evaluating projected foreclosure or modification scenarios. If the modification does not pass the NPV Test,

then it will be referred to the appropriate MI Company. The major MI companies have agreed to develop a mechanism by which they will pay partial claims where they deem appropriate to avoid foreclosure.

Servicers having at least a \$40 billion servicing book will have an option to substitute a set of Cure Rates and Re-default Rates estimated based on the experience of their own aggregate portfolios.

FHA, VA and rural housing loans will be addressed through stand-alone modification programs run by those agencies. FHA's Hope for Homeowners refinancing program will also be included in a parallel incentive program.

HARP (Home Affordability Refinance Program)

Many homeowners pay their mortgage on time but are not able to refinance to take advantage of today's lower mortgage rates. A Home Affordable Refinance through the Obama Administration's Making Home Affordable Program may help many of these homeowners who otherwise would be unable to refinance and whose loans are held by Fannie Mae or Freddie Mac refinance into a more affordable or more stable mortgage.

Eligibility

You may be eligible for a Home Affordable Refinance if you:

- Own a one-to four-unit home that is your primary residence;
- Have a mortgage owned or guaranteed by Fannie Mae or Freddie Mac;
- Are current on your mortgage payments and have not been more than 30 days late making a payment within the past 12 months;
- Have a first mortgage not exceeding 125 percent of the current market value of your home;
- Have income sufficient to support the new mortgage payments; and
- Can improve the long-term affordability or stability of your loan with the refinance.

Catch 22

Mortgage lenders may have additional underwriting overlays preventing the funding of this type of loans.

MERS (Mortgage Electronic Recording Systems)

MERS was developed in the early 1990s by financial institutions. Some of the majors were Bank of America, Countrywide, Fannie Mae, and Freddie Mac. MERS allowed the wholesale securitization of mortgage loans. The end result has been to avoid paying local governments their recording fees and to short circuit the intent of the recording laws designed to guarantee purchasers of mortgages a clean title. In addition the expansion of predatory lending occurred as a result of no longer being able to identify who the actual lender was or what the actual value of the underlying asset might be.

MERS serves as the mortgagee of record for lenders so mortgages can change hands without recording transfers. MERS is a nominee appointed to hold mortgages and facilitate transactions. There are at least two ways MERS Inc. a MERSCORP subsidiary becomes the nominated holder of a loan. The preferred way is to use a "MOM". MOM stands for "MERS as Original Mortgagee." Recent court opinions stress that this defect is a substantive failure and one that is fatal to a lender's legal ability to foreclose.

Over 62 million mortgages are now held in the name of MERS. A California bankruptcy court (Case No. 10-21656-E-11), following landmark cases in other jurisdictions, in early 2010, held that this electronic shortcut makes it impossible for banks to establish their ownership of property title and therefore to foreclose on mortgaged properties.

These opinions are being used to challenge any foreclosure in California based on a MERS assignment. Borrower's legal representatives are using these findings to obtain a temporary restraining order against a trustee's sale as well as a preliminary injunction barring sale of the subject pending litigation filed by borrowers challenging foreclosures based on a MERS assignments. These opinions may also serve as precedent in other jurisdictions, since the courts have cited non-bankruptcy cases related to the lack of authority of MERS.

Over the last several years' (prior to 2010) filings against MERS were based on the inability to produce the original note or assignment. The majority of courts considered this only a procedural defect. Recent cases are based on something substantive. If MERS is not the title holder of properties held in its name, the chain of title has been broken, and no one may have right to sue. Recently brought to light, is a practice of backdating assignments after foreclosure has been filed. Not only is this perjury, but is a prosecutable offense.

Quiet title actions are being filed in an effort to get homeowner's full title to their homes or as strategy for helping homeowners delay or even prevent foreclosure. On July 26, 2010, a class action was filed in Florida against MERS. It alleges that MERS is an artifice used to circumvent the judicial process and is used in a way that disguises who is receiving the benefits of the mortgage payments.

Qui tam actions allow for a private party to bring suit on behalf of the government for fraud. (State of California ex rel. Barrett R. Bates, filed May 10, 2010.) The suit states that "MERS claims to have 'saved' at least \$2.4 billion dollars in recording costs, otherwise accruing to local governments. The plaintiff sues for treble damages for all recording fees not paid during the past ten years, with civil penalties from \$5,000 and \$10,000 for each underpaid recording fee.

The problem on the table is the contractual right of investors in mortgage bonds to require banks to buy back loans at face value if there was fraud in the origination process. The aggregate value of the loans in question is substantial beyond available capital reserves of the largest U.S. banks combined. Investor lawsuits could cost banks billions. If courts decide to take up the consumer cause, millions of home mortgages could be deemed uncollectable and no longer on the books of some largest banks in the nation. Absent these sizable assets, the banks could become insolvent. While courts are not likely to let 62 million homeowners have their homes free and clear, the MERS title defect could give them significant leverage at the bargaining table.

Making Home Affordable Program Changes

The Making Home Affordable Program was intended to become less cumbersome on June 1, 2010. The U.S. Treasury Department announced it was streamlining the program to increase the number of successful home loan modifications.

It was originally intended that borrowers would first be placed in a trial modification plan and then produce financial documentation for qualification. Starting June 1, 2010, banks and mortgage companies participating in the program were required to collect all borrower documents needed with the initial application.

Another change stated change to the program is that applicants will need only to submit their last 2 paystubs and assigned form 4506-T allowing the lender to retrieve a copy of the applicant's tax transcript from the IRS.

Although these are stated changes, most lenders continue requiring substantially more documentation to open a HAMP or HAFA request. Often, a borrower initially meeting requirements for modification has had to re-submit required documents multiple times during the process, due to excessive time constraints from mortgage servicers who are overloaded with requests.

Current Foreclosure Issues

Many foreclosures are initiated by processors who receive high fees for foreclosing and have no incentive to pursue other workouts solutions. Servicers are supposed to work to minimize losses for the investors. Servicers were not adequately staffed to handle the surge in problem loans. For these servicers, it is not always possible to recoup the costs associated with staff increases and systems changes needed for workouts. Recouping costs by just foreclosing on properties has been straightforward.

Corner-cutting by mortgage servicers trying to keep costs down in dealing with the deluge of rising delinquencies and foreclosures created defects in documentation increases. Consumer awareness of this problem could increase the costs of foreclosure and decrease the valuation of mortgage loans. Headlines about flawed foreclosures have added momentum for the small group of investors who have been threatening legal action for years against the banks.

Lower wages and fewer workers are continuing to put downward pressure on house prices. The Congressional Budget Office doesn't expect the jobless rate to reach 5% until 2016. An earlier Bureau of Labor Statistics estimate was that it would not drop below 8% until late 2013, so these two agencies seem to be in general agreement on what the 'recovery slope' looks like.

High second mortgage balances coupled with declining home values leave many homes owners with negative equity. A drop in household income is placing many home owners behind the 8 ball and unable to afford their mortgage payments. With increased supply and decreased demand it will take years for the housing market to gain equilibrium.

Emerging Regulatory/Legislation Developing

Too Big to Fail/Volcker Rule: Neither the House nor Senate versions of the reform deal with institutional size. The Dodd Bill contains the "Volcker Rule," prohibiting firms from participating in some activities. No later than 15 months after the bill goes live, Federal banking agencies will issue rules prohibiting proprietary trading pertinent to investing or sponsoring hedge funds or private equity funds. Market-making or customer facilitation, trading or investing in government agency and municipal securities are exempted.

Resolution Authority: The creation of a three party bankruptcy panel, which could authorize the Treasury Secretary to appoint the FDIC as a receiver if large institutions become insolvent. Its goal is to provide a better way to resolve large, failing institutions. The hope is to avoid another Lehman Brothers fiasco.

Bureau of Consumer Financial Protection: An agency independent from, yet still within, the Fed. The agency is charged with creating and enforcing rules over institutions offering financial products or services that could have a substantive impact on a consumer.

In the House Bill the SEC will require broker-dealers to have a fiduciary responsibility to their clients. The Dodd Bill requires the SEC to examine existing standards of disclosure. From those findings, the SEC is then required to create fiduciary duty guidelines.

Derivatives: Senate Agriculture Committee approved a bill that requires the over-the-counter derivative contracts used by AIG, which are like those sold by Goldman Sachs to AIG. The bill requires all such trades be cleared through the exchange. The goal is to make public nature of the value and/or risk of such activity. This could result in commercial banks being prohibited from trading through their own swap desks. Look for intense lobbying for exemptions.

Wall Street Reform and Consumer Protection Act: Requires shareholder approval of executive compensation and “golden parachute” compensation.

Money Market Funds: Reform of money market funds may push investors to less regulated investment vehicles, which would create a systemic risk. The President’s Working Group (PWG) directs that the Financial Stability Oversight Council (FSOC) established in the Wall Street Reform and Consumer Protection Act, work with the Securities and Exchange Commission, as the regulator of money market funds. These options range from authority currently available to the SEC to changes that would require new legislation.

Options for Home Owners Who do not qualify for HAMP

Forensic loan audits can be performed. A forensic audit is an audit of a borrower's financial reports and documents that is designed to find and expose the common mistakes and laws broken by the lenders in the ruthless lending processes during the origination of the loan. After the audit is completed and a report is made, it is used to significantly help the borrower in the financial negotiation efforts with the lenders.

Forbearance agreements are agreements made between a mortgage lender and delinquent borrower in which the lender agrees not to exercise its legal right to foreclose on a mortgage and the borrower agrees to a mortgage plan that will, over a certain time period, bring the borrower current on his or her payments. Often, this results in an increase to the existing payment.

FHA partial claims can be executed where homeowners receive an interest free, HUD guaranteed, loan that pays off arrearage and reestablish the existing 1st lien. The loan is paid back when the 1st mortgage is paid off, or when the house is sold. Qualifications for the partial claim require homeowners to have the following:

1. Long term ability to make regular payments and pay back the loan.
2. Homeowners who are not capable of qualifying for a workout plan or a forbearance agreement.
3. Provide proof the financial hardship is over and was only temporary.
4. Homeowner needs to remain on the property and keep it in satisfactory livable condition.
5. The existing mortgage loan should be at least four months overdue, but no longer than twelve months.

Lender Internal Modification Programs are also available and are based on the Lender's discretion and vary widely between lenders.

Chapter 13 Bankruptcy is available to homeowners as an alternative to foreclosure. Often, homeowners who are struggling to make their housing payments and have already ceased paying other debt obligations, find it difficult to begin repaying their other debt obligations, mortgage arrearage, and continue to make regular monthly mortgage payments. This can lead to a vicious cycle, often ending in dismissal of the Bankruptcy and risk of foreclosure.

Traditional Short Sales allow borrowers to sell the home in a short sale, if:

1. they have a hardship, such as a job loss, divorce or medical emergency
2. owe more than your house is worth
3. are unable to afford the current monthly mortgage payment
4. are unable to modify the current home loan

Sometimes all retention alternatives are exhausted and the only available option is to liquidate the property using a Short Sale to avoid foreclosure. Failed Short Sales can often be concluded as a Deed in Lieu of Foreclosure, but many Lenders are only willing to take the Deed in Lieu after all other retention options are exhausted.

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