



# The Future of Loss Mitigation

**BEYOND COVID-19: NECESSARY REFORMS TO PRESERVE PANDEMIC INNOVATION**

Mortgage servicers are the most important conduit for relief for distressed borrowers and the primary means by which they can recover financially and remain in their homes. To accomplish this, servicers must have the resources to ensure borrowers receive timely and durable assistance to avoid foreclosure. Informed by guiding principles, policymakers must preserve the critical features mortgage servicers implemented throughout the COVID-19 pandemic. Further action by policymakers to reform the loss mitigation standards to service loans in default is required to aid borrowers unable to afford their payments given evolving market conditions.

# Background

Throughout the COVID-19 pandemic, mortgage servicers delivered effective payment relief to over 7.5 million borrowers industry-wide through a COVID-19 forbearance.<sup>1</sup> To assist borrowers, servicers advanced their own funds to meet the statutory obligations of the Coronavirus Aid, Relief, and Economic Security (CARES) Act and the requirements of Fannie Mae and Freddie Mac and the Federal Housing Administration (FHA), Department of Veterans Affairs (VA), and the Rural Housing Service (RHS).

The government insurers and guarantors expanded the use of products that have now become household names — forbearance, partial claim<sup>2</sup>/payment deferral, and extended term modifications. These expanded toolkits allowed mortgage servicers to offer solutions to borrowers to either maintain their current payments or achieve a reduced monthly mortgage payment. Many of these flexibilities are temporary, tied to the existence of the CARES Act national emergency, or a hardship due to COVID-19. Some have already expired. Therein lies the challenge, particularly with the expected expiration of the national emergency.

The economy changed significantly throughout 2022. Our industry must consider how to deliver effective payment relief in today's higher-interest rate environment, in contrast to the low-interest rate environment that characterized the pandemic housing and refinance boom. The prevailing note rates in the mortgage securities issued by the GSEs and Ginnie Mae are much lower than today's market rates. The usual solution and greatest contributor to helping borrowers achieve a new affordable payment — a modification that changes the borrower's loan terms by either extending the loan's maturity date and/or reducing their contractual interest rate to the market rate — is ineffective to drive payment reduction. At the same time, home prices are beginning to decelerate after two years of significant appreciation, eroding the strong equity positions of homeowners and potentially leaving some borrowers underwater.

The pandemic undoubtedly provided policymakers with a roadmap on how to respond to future emergencies and natural disasters. The swift change in the market also demonstrated the importance of ensuring servicers have durable solutions in their toolkits to help borrowers through any hardship.<sup>4</sup>

The Mortgage Bankers Association (MBA) has considered how the COVID-19 pandemic should shape permanent loss mitigation policy. This paper provides a comprehensive outlook on the necessary policies to best preserve affordable homeownership for struggling borrowers and to protect communities. Considering the lessons learned from the pandemic and the challenges in today's high-interest rate environment, policymakers must prioritize the principles of simplicity, standardization, and sustainability to guide their decisions to reform default loss mitigation servicing ahead of the next adverse market event.

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1. MBA's Monthly Loan Monitoring Survey, September 2022.

2. The Department of Agriculture's (USDA) Rural Housing Service refers to a partial claim as a Mortgage Recovery Advance.

3. Ginnie Mae issuers of mortgage-backed securities participate in the Federal Housing Administration (FHA), the Department of Veterans Affairs (VA) Home Loan Guaranty, and Department of Agriculture's (USDA) Rural Housing Service programs.

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4. "Traditional" or "standard" reasons a borrower may face a financial hardship can vary. Common examples that lead to a reduction in a borrower's income or an increase in a borrower's expenses are the death of a co-borrower, divorce, disability, or unemployment.

# Principles to Guide and Preserve Pandemic Innovation

For loss mitigation policy to be successful, it must maximize the number of borrowers that can retain their homes while reducing the loss exposure to the risk holders (GSEs, FHA, VA, and RHS). Therefore, policies must quickly qualify the most borrowers and help those borrowers achieve favorable outcomes to remain in their homes.

To do so, policymakers must preserve the critical features, processes, and positive borrower experience servicers have created throughout the pandemic. The following principles strike the proper balance between providing engaged borrowers with access to practical solutions that resolve a borrower's delinquency, reducing the loss exposure to credit risk holders, and ensuring mortgage servicers can maintain operational efficiency (i.e., scalability) as defaults rise.

Loss mitigation has become increasingly complex for mortgage servicers and borrowers. As a result, servicers have invested heavily in consumer education and self-service technology. Importantly, these advancements have allowed borrowers who have engaged with their servicer to easily receive the assistance they need, while allowing servicers to deploy exhaustive outreach strategies to establish contact with borrowers who have yet to engage.

Accordingly, these guiding principles should identify the most important features that should be preserved across the GSEs and the federal agencies.

## SIMPLICITY

Loss mitigation must reduce administrative burdens and barriers for borrowers to qualify quickly for a home retention solution. Those barriers include the process to complete the loss mitigation solution, the eligibility to qualify for the solution, and the terms the borrower is expected to follow. The lessons of past crises are clear that simplicity provides accessibility. Borrowers receive the benefits of loss mitigation when servicers can provide home retention solutions that borrowers can easily understand, thereby reducing unnecessary consumer confusion throughout the process.



To advance the principle of “simplicity,” loss mitigation policy must:

### **LIMIT REQUIRED DOCUMENTATION TO ENCOURAGE SERIOUSLY DELINQUENT BORROWERS TO QUALIFY FOR A PERMANENT SOLUTION**

An unnecessary paper chase can delay or prevent a borrower from qualifying for a home retention option.<sup>5</sup> Thus, FHA, VA, and RHS must change their regulations or guidelines to follow the Enterprises' lead on reduced documentation standards. Seriously delinquent borrowers with accumulated arrearages and negative credit consequences are often unresponsive to servicers' efforts to establish contact. Once contact is established, limiting the documentation required for borrowers to qualify for a permanent solution has proven effective to quickly providing payment relief to borrowers.

5. The top fallout reason under HAMP was a failure to complete the package. See Footnote 9.

## STANDARDIZATION

Mortgage servicers should be able to provide borrowers with a consistent loss mitigation experience, regardless of the underlying reason for hardship or who insures or guarantees the loan. This experience includes an aligned loss mitigation framework between the GSEs and the government agencies. Most of all, standardization allows servicers to communicate and educate borrowers most consistently and clearly on how the loss mitigation process works. With a unified approach, servicers will ensure that borrowers with the same circumstances do not receive a disparate experience when qualifying for a potential



solution.

To advance the principle of “standardization” and build upon the principle of “simplicity,” loss mitigation policy must:

### CONSISTENTLY RESOLVE TEMPORARY HARDSHIPS WITH PAYMENT DEFERRALS AND PARTIAL CLAIMS.<sup>6</sup>

The collaboration between the GSEs and the government agencies regarding the aligned use of the payment deferral and partial claim should continue and capitalize on the success of the pandemic that proved these two options as the most common and successful ‘post-forbearance’ solution. Specifically, the GSEs should expand the

6. A partial claim allows mortgage servicers to recover corporate funds that have been advanced to meet servicers obligations to Ginnie Mae and cure a borrower’s delinquency from the agency (FHA, VA, and USDA). Borrowers, in turn, execute a subordinate lien and promissory note promising to repay the partial claim advancement to the agency at payoff, refinance, or maturity. Borrowers are only able to receive up to 30% of the unpaid principal balance at the time of the original default. The GSE payment deferral functions similarly and leads to the same result for borrowers. However, unlike Ginnie Mae servicers, GSE servicers are only required to advance principal and interest on behalf of the borrower for four months. When completing a payment deferral, the missed payments are ‘deferred’ or added to the end of the loan, which the borrowers also agree to repay at payoff, refinance, or maturity. A servicer does not file a claim with Fannie Mae or Freddie Mac for the delinquency. A borrower only executes a deferral agreement, not a subordinate lien or promissory note.

payment deferral beyond reinstating borrowers in rolling delinquency (i.e., the borrower has returned to making regular payments but is unable to reinstate their loan). Likewise, the government agencies should preserve the partial claim ahead of a modification in the loss mitigation waterfalls. The alternative option for borrowers is a repayment plan, which requires a borrower to contribute additional income to cure their delinquency. Industry data has shown that repayment plans are unsustainable.

Loss mitigation policy should continue to distinguish between short-term versus long-term hardships. As standalone products, payment deferral and partial claim offer able borrowers the opportunity to cure their arrearage and resume their regular monthly payments quickly. Providing a solution to temporary hardships via payment deferral or partial claim ensures that borrowers who need payment reduction will complete a modification only when a modification offers a better outcome. Notably, a payment deferral and partial claim are effective in a rising rate environment.

### STANDARDIZE POLICY TO OFFER EXTENDED TERM MODIFICATIONS ONLY AS NECESSARY

Extended modification terms erode a borrower’s equity and increase performance costs. Therefore, servicers should offer borrowers extended modification terms when necessary to preserve homeownership.

To align more closely with GSEs, the government agencies must offer borrowers the opportunity to extend their loan term up to 480 months (or 40 years) from modification. Extended modifications offer borrowers an additional opportunity to achieve an affordable payment when a standard modification term of up to 360 months (or 30 years) does not. These can also be a valuable solution for servicers to offer borrowers whenever market rates are significantly above prevailing note rates.

Conversely, to ensure closer alignment between the agencies, the GSEs should allow servicers to offer borrowers a traditional 360-month (or 30-year) modification term if a borrower can achieve an affordable payment without an extended term modification. This may result in the borrower paying less interest over the life of the loan.

### MAINTAIN A CONSISTENT USE OF TARGETED PAYMENT RELIEF FOR MODIFICATIONS

When reviewing a borrower for a modification, especially when combining with a partial claim to defer additional principal, the objective must remain to provide the borrower with sufficient payment relief to avoid redefault, while providing investors/guarantors with a less costly resolution than a non-retention option like deed-in-lieu

or foreclosure. Research has consistently shown that the greater the payment relief a borrower can achieve, the more sustainable their payment is and the less likely the borrower will redefault in the future.

After more than two years of widespread adoption of streamlined applications, the government agencies should maintain their alignment with the Flex Modification and continued use of a targeted payment reduction of 20% of principal and interest. Generally, the delinquency rates of the government agencies are higher than the GSEs. As equity positions continue to erode, deliberately targeting a decrease in the borrower's principal and interest payment will help borrowers achieve a more favorable and sustainable outcome for long-term performance.

## **SUSTAINABILITY**

Loss mitigation solutions must help borrowers achieve an affordable payment for the long term and decrease the risk of redefault. Home retention solutions must be in the best interest of the borrower, the servicer, and the investor/insurer/guarantor. For borrowers that need payment relief, modifications must decrease a borrower's monthly mortgage payment to help the borrower into a better financial position than before the default episode occurred.

To ensure servicers can deliver effective assistance to borrowers, loss mitigation solutions must also be operationally feasible for servicers to implement. Sustainable policymaking ensures that servicers have the clarity to update processes and technology, and the necessary implementation time to meet the mandatory compliance deadline. To accomplish these goals, policymakers must provide transparency and the opportunity to partner with stakeholders in the design of final policy, especially when final policy affects a servicer's interaction with borrowers and becomes more complex.

Together, the loss mitigation policies and framework outlined above also advance the principle of "sustainability." All seek to ensure a borrower can achieve a favorable outcome by either resuming their regular monthly payment or reducing their payment so the borrower can remain in their home with as few hurdles as necessary.

To summarize, default servicing is about maintaining a relationship with a borrower to help them through financial hardship and having the resources to be successful. Those resources include providing mortgage servicers with access to all available loss mitigation tools to help borrowers resolve their delinquency and retain their homes. As we look forward, the regulatory framework must also change to respond to evolving market conditions.

# The Future of Loss Mitigation

Policymakers must provide the certainty necessary for the industry to transition beyond the pandemic by addressing two issues: 1) the necessary extension of the successful “temporary flexibilities” into permanent solutions and 2) loss mitigation in a high-interest rate environment. It will be essential for Congress, the administration, and policymakers at all levels to take the coordinated actions necessary to ensure that servicers can continue to support struggling borrowers.

For the GSEs, advancing the principles outlined above for loss mitigation in a high-interest rate environment is straightforward. Borrowers that need to achieve a lower payment will be able to do so with additional adjustments to the existing framework of the Flex Modification. For borrowers serviced under Ginnie Mae programs (FHA/VA/RHS) there is no ideal solution currently available that can be leveraged today.

While “forbearance” has in some ways become synonymous with pandemic servicing, this paper will not focus on forbearance in the context of the future of loss mitigation. Forbearance is an excellent option for borrowers facing temporary hardship. Forbearance allows borrowers to reduce or suspend their regular monthly payments. Importantly, forbearance can help mortgage servicers establish ongoing contact with a borrower to identify the most appropriate solution to resolve a borrower’s delinquency at the end of forbearance.

While forbearance played an instrumental role throughout the COVID-19 pandemic, our recommendations are primarily focused on the “post-forbearance” loss mitigation options. These options resolve delinquencies, but do not necessarily require forbearance to qualify for a home retention solution.<sup>7</sup> Forbearance does not resolve delinquencies, and therefore requires a resolution at the end of the forbearance term.<sup>8</sup>

## NECESSARY POLICY REFORMS FOR SERVICING BORROWERS IN DEFAULT

The following are roadblocks that must be eliminated by stakeholders in the government guaranteed loan programs so mortgage servicers can continue to deliver effective default services for borrowers and be prepared as defaults rise. In priority order, for loss mitigation policy to be successful:



## THE VA MUST IMPLEMENT A PERMANENT PARTIAL CLAIM PROGRAM

The Veterans Assistance Partial Claim Program (VAPCP) successfully allowed servicers to offer veteran borrowers impacted by the COVID-19 pandemic the ability to add missed payments to the end of their mortgage as a non-interest-bearing lump sum payment. VA would then reimburse the servicer who made the required advances on the borrower’s behalf from the veteran’s guarantee.

7. VA Partial Claim Program, U.S. DEPARTMENT OF VETERANS AFFAIRS, available at [https://www.benefits.va.gov/HOMELOANS/partial\\_claim.asp](https://www.benefits.va.gov/HOMELOANS/partial_claim.asp) (showing the VAPCP did, for example, require a forbearance to qualify for a partial claim. A principle of loss mitigation is that a borrower is not required to receive a forbearance to qualify for a home retention solution.)
8. Exit Your Forbearance, CONSUMER FINANCIAL PROTECTION BUREAU, available at <https://www.consumerfinance.gov/coronavirus/mortgage-and-housing-assistance/help-for-homeowners/repay-forbearance/> (explaining that borrowers are also permitted to submit a lump-sum payment at the end of forbearance to reinstate their delinquency, but are not required to do so).



However, today mortgage servicers are unable to provide veteran borrowers facing financial hardship with a standalone partial claim under VA's loss mitigation program. In fact, the VAPCP, designed by emergency regulatory authority solely to help borrowers impacted by the COVID-19 pandemic, expired on October 28, 2022. Additionally, the VA Refund Modification, VA's specific modification program that is combined with a partial claim to help borrowers achieve payment reduction when exiting a COVID-19 forbearance, will expire on July 1, 2023.

In the absence of a partial claim, mortgage servicers will return to utilizing VA's standard preferred order of loss mitigation options that are not affordable for many borrowers, especially in high-interest rate environments. To help borrowers that need payment reduction today, the VA will have to expand its Refund program, as a means of last resort.

Action by Congress is likely necessary to fund and authorize a permanent partial claim program. Absent such funding, a long-term partial claim program could adversely affect the larger VA Benefits Administration through high costs. A potential consequence could be an increase in VA's funding fee for new applicants.

Preventing foreclosure for borrowers should not increase the cost of credit for new borrowers. Without such action by Congress and the VA, mortgage servicers will not be able to provide effective, long-term payment relief to borrowers as defaults rise. The loss mitigation solutions available to veteran borrowers should be offered as a benefit to participation in the VA loan guaranty program. Once implemented, the VA can redesign the partial claim and align more closely with FHA's existing practices. Veteran borrowers should

have loss mitigation options that are at least as effective as those available to other government-insured borrowers.

### **THE CONSUMER FINANCIAL PROTECTION BUREAU (CFPB) MUST MODERNIZE REGULATION X TO CREATE FLEXIBILITY AND IMPROVE THE BORROWER EXPERIENCE**

The CFPB's servicing rules were designed after the wave of foreclosures that happened after the 2007-2008 financial crisis. They were designed to reflect the dominant loss mitigation paradigm at the time, primarily the Home Affordable Modification Program (HAMP). HAMP was a document intensive program that required a paper chase from the borrower and difficult evaluations by the servicer. Consequently, borrowers often failed to complete the packages necessary for relief, and some servicers struggled to implement portions of the program at scale.<sup>9</sup>

The CFPB's loss mitigation servicing rules reflect this experience. They are heavily procedural and create rigid evaluation paradigms that make it difficult for servicers to offer streamlined options or an initial period of forbearance without a formal evaluation of the borrower's financial circumstances. While the CFPB rules are appropriately focused on process rights rather than entitlements to investor outcomes, these rules often drive how the other government investor or guarantors can design their loss mitigation solutions.

9. One Mod: Principles for Post-HAMP Loan Modifications, Mortgage Bankers Association (2016), Table 4, Appendix 1, available at <https://nysba.org/NYSBA/Coursebooks/Fall%202016%20Coursebooks/Mortgage%20Foreclosures%20and%20Workouts/One%20Mod%20-Principles%20for%20Post-HAMP%20Loan%20Modifications.pdf> (showing that, according to Treasury data, the top HAMP denial reason was for insufficient documentation).

The CFPB should modernize Regulation X to clearly and unambiguously allow mortgage servicers to continue to qualify borrowers for a partial claim/payment deferral and modification based on an incomplete application when permitted by agency or investor guidance. The exceptions that servicers relied upon throughout the past two years to qualify borrowers for a permanent solution are largely focused on borrowers with a COVID-19 hardship. A clearer, more flexible regulatory structure that broadly permits servicers to offer streamlined options — regardless of an individual borrower’s hardship type or the qualifying hardship reasons generally permitted for a particular streamlined option — eliminates any uncertainty and frees up the agencies and other investors to redesign their waterfalls to reflect the lessons learned from the COVID-19 pandemic.



Rulemaking will allow the CFPB to address two specific issues that restrict the feasibility of qualifying borrowers based on incomplete applications moving forward: 1) Eliminating reference to qualifying a borrower for a streamlined modification if the option is made available to a borrower with a COVID-19 hardship. Borrowers are already reporting non-COVID-19-related reasons for hardship, and the further from the pandemic we move, the less available this protection becomes. 2) Eliminating reference to qualifying for a payment deferral/partial claim if the covered amount is a result of a forbearance for borrower’s experiencing a COVID-19 hardship. Forbearance is not required to qualify for a partial claim or payment deferral. Other hardships, such as a natural disaster, are not covered either.

A more flexible regulatory framework will also ensure servicers have the necessary compliance protections as the agencies promote streamlined applications, regardless of a reason for hardship. The loss mitigation experience is continuing to evolve as servicers engage with borrowers through digital and traditional means, including reviewing borrowers for permanent solutions through telephone conversations once contact is established. A reformed Regulation X can capture this evolution away from the document chase, improve the borrower experience, and

reduce instances of unnecessary consumer confusion. For example, a servicer should not be required to send a possibly alarming early intervention letter to borrowers on forbearance.

Regulation X was crafted to ensure that servicers provided sufficient protections to consumers to prevent foreclosure and worked with those borrowers that had engaged with the servicer. Modification offerings, the loss mitigation toolbox, and technology have advanced significantly over the years to facilitate streamlined modifications. The time is right to review Regulation X’s rigid standards that have caused consumer and servicer confusion alike and now inhibit servicers from delivering an effective loss mitigation process for borrowers.

### **FHA SHOULD PERMANENTLY UPDATE ITS LOSS MITIGATION POLICY IN THE HUD HANDBOOK**

We encourage FHA to formally update HUD Handbook 4000.1, *FHA Single Family Housing Policy Handbook*, as quickly as possible and make permanent the COVID-19 Recovery Loss Mitigation Options. FHA’s recent announcement of Mortgagee Letter 2023-02, *Expansion of the COVID-19 Recovery Loss Mitigation Options*, is a welcomed step in the right direction to preserving the critical loss mitigation features after pandemic. Allowing mortgage servicers to continue offering borrowers the COVID-19 protections for any hardship is important. However, according to FHA’s Mortgagee Letter, servicers may not offer the COVID-19 Loss Mitigation Options after October 30, 2024. FHA should work to ensure these so-far successful options are permanently secured.

### **POTENTIAL SOLUTIONS FOR TODAY’S HIGH-INTEREST RATE ENVIRONMENT**

As noted, modifications are generally ineffective to provide payment relief in today’s high-interest rate environment, where borrower’s note rates are overwhelmingly exceeded by prevailing interest rates. This issue underscores the importance of having durable solutions in place that work through all economic climates.

As mentioned, providing payment relief for borrowers that need a lower payment is easier under the existing structure of the GSE’s Flex Modification given the accessibility of levers that drive payment reduction. It’s more challenging for borrowers under the Ginnie Mae programs. In short, the issue is a matter of liquidity risk to meet ongoing financial obligations when borrowers are unable to make their monthly payments. The GSEs bear the cost when a borrower completes a modification. Under Ginnie Mae’s programs, the servicer bears much of the cost.



## GOVERNMENT-SPONSORED ENTERPRISES (FANNIE MAE AND FREDDIE MAC)

The Flex Modification has generally been effective at providing borrowers with access to all available levers to drive payment reduction — interest rate reduction, term extension, and principal forbearance. In today's high-interest rate environment, term extension to 480 months (or 40 years) is generally the only lever available and may not always help borrowers achieve the target payment. For borrowers to utilize additional forbearance, a borrower's post-modification Market-to-Market Loan-to-Value (MTMLTV) ratio must be greater than 80%. The strong equity positions of borrowers make this lever inaccessible, but paper gains in equity may not result in available funds to save their homes.

## ALLOW ADDITIONAL PRINCIPAL FORBEARANCE FOR BORROWERS WITH LESS THAN 80% MTMLTV RATIOS

The GSEs should evaluate the feasibility of expanding their MTMLTV ratios. Understandably, MTMLTV thresholds were designed to test the net present value to ensure the cost of providing a modification to a borrower did not exceed the cost of foreclosure at the portfolio level, thereby protecting the GSEs and taxpayers from avoidable losses. Servicers are only obligated to advance the borrower's missed payments to the GSEs for up to four months. Evaluating the feasibility of lowering the MTMLTV strikes the proper balance between providing payment relief to delinquent borrowers and managing the loss exposures of the GSEs.

## GINNIE MAE (FHA, VA, AND USDA)

Ginnie Mae servicers do not have the tools to provide payment relief to borrowers in today's high-interest rate environment.<sup>10</sup>

Simply put, Ginnie Mae issuers are required to buy loans out of the pool when completing a modification (i.e., repurchase them). That is because Ginnie Mae does not allow loans to have the term extended or be "reamortized" while in the existing mortgage-backed security (MBS). When an issuer repurchases a loan out of the MBS, they do so with their own funds.<sup>11</sup>



The result at an individual level is that a borrower's payment may increase when modifying a loan to the market. This is unworkable for most borrowers recovering from a financial hardship. At the macro level, servicers cannot carry the cost to repurchase loans to modify borrowers to a new payment the borrower cannot afford. Yet, servicers are required to review a borrower for and potentially complete such a modification in today's high-interest rate environment.

Thus, the specific objective is to mitigate liquidity risk while providing payment relief to keep borrowers in their homes and the loan in Ginnie Mae's security.

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10. A deeper dive into potential solutions to structural reforms to Ginnie Mae to ensure sufficient servicer liquidity is merited given existing market conditions. Being prepared when defaults rise is necessary to ensure mortgage servicers can maintain operational scalability and provide payment relief to borrowers. MBA is engaging in this work, but a detailed discussion of such reforms is beyond the scope of this paper.

11. Tozer, The Mortgage Interest Rate Increase Requires a Reevaluation of Loss Mitigation Techniques, Urban Institute (Aug. 10, 2022), available at <https://www.urban.org/urban-wire/mortgage-interest-rate-increase-requires-reevaluation-loss-mitigation-techniques> (noting in previous publications that, in addition to the market rate the loan must be modified to, the final interest rate a borrower receives is tied to the cost of funds an issuer bears).

# Recommendations

To help the maximum number of borrowers achieve the target payment reduction, the following proposals are MBA's recommended loss mitigation solutions for high-interest rate environments.

## 1. RECAST

For FHA and USDA borrowers with partial claim funds available, a recast allows a borrower to reduce their payment by reamortizing their loan at the remaining term and at the existing rate after curing a borrower's arrearage and deferring additional principal. The servicer would be allowed to keep the loan in the MBS. This is like the current structure of the Flex Modification that currently requires servicers to modify a borrower's loan at the lower end of the existing rate or the modification rate (if a borrower's post-modification MTMLTV ratio is greater than 80%). This proposal has been submitted repeatedly throughout the years.<sup>12</sup>

However, Ginnie Mae's mortgage-backed securities Prospectus prohibits reamortization of loans while in security. Any change to Ginnie Mae's Prospectus would only apply prospectively for new securities, not retroactively. Therefore, Ginnie Mae recasts are not viable for today's delinquent borrowers.

Ginnie Mae should continue to explore changes to its Prospectus to make recasting a viable option in the future. Ginnie Mae recasts most ably offer servicers a solution for borrowers that is simple and sustainable.

## 2. PAYMENT SUPPLEMENT ACCOUNT/ PARTIAL CLAIM BUYDOWN

A potential alternative for FHA and USDA is the Payment Supplement Account (PSA), which is essentially a partial claim buydown.<sup>13</sup> In its most basic form, a servicer would receive partial claim funds from FHA or USDA and place them in a custodial account. On a monthly basis, a servicer would draw from the custodial account to supplement the borrower's principal portion of their monthly payment.



A servicer would continue to supplement the borrower's payment from the custodial account for a defined term.

Until the final policy is received from FHA or USDA, the appropriate next step is for the agencies to release proposed policy on the drafting table, or operate a pilot program, before permanently implementing and requiring this solution. By its nature, managing custodial funds over time is a new function for servicers and one that is operationally complex. Providing transparency ensures all interested stakeholders can completely analyze the new policy and understand potential risks and implementation hurdles. For example, work must be undertaken in advance to ensure that disclosures will be updated to ensure the borrower understands the conditions and how they're expected to perform.

While the PSA is viable, the challenges illustrate the complexity of delivering loss mitigation in a high-interest rate environment. Most importantly, the PSA allows servicers the opportunity to maintain a relationship with borrowers and assist those homeowners that may be struggling to afford their payment.

12. Id.; Government Loan Modifications, Urban Institute (Jan. 2018), available at [https://www.urban.org/sites/default/files/publication/95671/government-loan-modifications\\_5.pdf](https://www.urban.org/sites/default/files/publication/95671/government-loan-modifications_5.pdf).

13. Payment Supplement: A Loss Mitigation Option to Provide Payment Relief for FHA Loans in a High Interest Rate Environment, Center for Responsible Lending, Housing Policy Council (Nov. 11, 2022), available at <https://www.responsiblelending.org/research-publication/payment-supplement-loss-mitigation-option-provide-payment-relief-fha-loans-high>

### 3. PORTFOLIO



Additionally, the agencies, including Ginnie Mae, should explore their authority to purchase loans from servicers and hold them in their own portfolios when a loss mitigation solution using standard tools is unavailable for a borrower. The VA is currently pursuing this path by considering an expansion of their Refund Program (a new VA Purchase Program).

A partial claim may not be available for all borrowers, either because the borrower has exhausted their maximum allowable or the program does not exist. By moving a loan into their portfolio, the agency can conduct additional loss mitigation solutions that are not otherwise available, such as additional interest rate reduction or principal forgiveness, to help borrowers remain in their homes. Moving a loan into an agency's portfolio is not a preferred solution, but may be necessary in the future if action is not taken to reform the VA partial claim, implement the PSA, and eliminate barriers to permit recasts. For FHA, this may include renewing the Single-Family Loan Sale.

### SUMMARY

Our industry faces several challenges to preserve affordable homeownership. To meet those challenges, policymakers must prioritize the principles of simplicity, standardization, and sustainability to preserve the flexibilities that mortgage servicers leveraged to assist struggling borrowers. Immediate action on the recommendations discussed above by Congress, CFPB, and FHA are all necessary to ensure long-term reform of default servicing policy.

#### Potential Government Loss Mitigation Waterfall

Home Retention Options	Modification Waterfall	
<p><b>REPAYMENT PLAN</b></p> 	<p><b>30 YEARS</b></p>	<ul style="list-style-type: none"> <li>• Standalone Modification (term extension)</li> <li>• Modification with partial claim (term extension + arrearage)</li> <li>• Modification with partial claim (term extension + arrearage + principal deferment)</li> </ul>
<p><b>PARTIAL CLAIM</b></p>  <p><b>MODIFICATION</b></p>		<p><b>40 YEARS</b></p>

# Summary of Recommendations

## **ALL**

- Provide transparency throughout the policymaking process to allow the opportunity for stakeholders to provide thoughtful design feedback, including on implementation hurdles and timeframes.

## **GSE**

- Expand the payment deferral to resolve temporary hardships.
- Incorporate a 30-year modification into Flex Modification.
- Allow additional principal forbearance for borrowers with less than 80% post-modification MTMLTVs.

## **ALL GOVERNMENT PROGRAMS**

- Limit required documentation to encourage seriously delinquent borrowers to qualify for a permanent solution.
- Preserve the use of the partial claim to resolve temporary hardships and to combine with a modification.
- Consistently offer extended borrowers loan terms up to 480 months (or 40 years) from modification.
- Maintain use of targeted payment relief to ensure a borrower's new payment is affordable.

## **VA**

- Implement a permanent partial claim program.

## **FHA/USDA**

- Implement the Payment Supplement Account for today's high-interest rate environment.

## **CFPB**

- Reform Regulation X to unambiguously allow servicers to qualify borrowers for a loss mitigation option based on streamlined application and improve the borrower experience.

## **GINNIE MAE PROGRAMS (FHA/VA/USDA)**

- Change the Prospectus to allow borrowers to receive payment reduction with a recast.
- Move loans into a portfolio to offer borrowers additional opportunity to receive a home retention option only as a means of last resort.

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**For more information, contact:**

**Justin Wiseman**

Vice President, Managing Regulatory Counsel  
Mortgage Bankers Association  
jwiseman@mba.org

**Brendan Kelleher**

Associate Director, Loan Administration  
Mortgage Bankers Association  
bkelleher@mba.org