

# A Government Refinance Program Should Be Implemented Immediately to Help Borrowers who Lack other Options Keep their Homes

## MBA RECOMMENDS

The federal government should establish a refinance program to help reach more troubled borrowers, especially those who do not have other options available to them.

## BACKGROUND

During 2003 through 2006, home prices increased in many parts of the country at a pace that far exceeded inflation. As prices increased, many mortgages were written with adjustable interest rates and/or negative amortization features. In 2007, home prices in many of these same areas began to fall dramatically, triggering a market response that created record borrower defaults. The resulting glut of foreclosed properties coming on the market helped swell the homes for sale nationwide in 2008 from a normal 2.6 million units to 4.6 million units. This has further reduced real estate prices and caused a backlog of homes for sale in excess of one year's supply. Resetting adjustable rate mortgages (ARMs) and mortgage balances that exceed the home's value have, in many cases, limited homeowner options for managing their financial needs. The end result will be higher levels of foreclosures again in 2009, which will negatively impact housing prices.

While servicers have executed a record number of repayment plans and loan modifications to help borrowers in distress, servicers are limited in their borrower assistance options by the loans' investor contracts. The ability to amend investor contracts or obtain investor approval to exceed contractual limits has proven to be very difficult, slow and in some cases impossible. Government efforts to date to help servicers overcome the contractual barriers to modifying mortgages have fallen short of the need.

A clear, simple and effective government refinance program is needed to rescue mortgages that cannot be modified because they have been securitized into private label mortgage-backed securities (private label MBS); securitized into Fannie Mae, Freddie Mac or Ginnie Mae securities (government MBS); or are sitting in financial institution portfolios as whole loans (whole loans). The refi program should also assist borrowers who need to reduce their monthly mortgage obligation but are trapped in their current loan because their property value has fallen below the balance of their mortgage loan.

## COMPONENTS OF AN EFFECTIVE SOLUTION

In establishing a comprehensive refinance process, MBA urges the administration and Congress to consider the following core principles:

- The solution should allow for the refinancing of whole loans, loans in government MBS, and loans in private label MBS.
- The solution should bring borrower monthly payments down to a targeted maximum debt to income (DTI) ratio to make sure that the monthly payments are affordable by the homeowner.
- Borrowers should be required to consider loan modifications allowable by existing investor agreements before seeking any government assistance in the form of a refinance program.

- Servicers should utilize the following hierarchy for executing modifications:
  1. mortgage rate modifications;
  2. mortgage term modifications, and then, as a last resort,
  3. principal deferrals.
- Principal modifications should not unjustly enrich a borrower. Accordingly, principal modifications that postpone rather than forgive principal are always preferred.
- Any government refinance solution needs to have an immediate impact so it should require only executive branch authorization not new legislation.
- The program should avoid contractual barriers to refinance such as large principal write downs.

## PROVIDING MORE OPTIONS FOR BORROWERS

The government refinance program should encourage servicers to use the following decision process to determine the optimal refi/modification solution for borrowers that cannot be helped through other modification or refinance programs.

1. The servicer should first determine if a permanent loan modification within the legal constraints of existing

ownership structure (i.e. whole loan versus government MBS versus private label MBS) or a regular refinance of the mortgage would reduce the monthly payment to a level affordable by the borrower (as determined by a targeted DTI ratio).

2. If the borrower does not qualify for a regular refinance, then determine if a new government program rate/term refi would bring the loan down to a targeted DTI ratio. If so, the servicer should do a special rate/term refi. A special rate/term refi adopts the principles of a streamline refinance, whereby the current value of the property is not a barrier to getting a new loan with a lower payment.
3. If none of the steps above work, the servicer should utilize the new government program after determining the maximum loan amount that would create a mortgage with principal balance at 90 percent of the current property value and still provide for a targeted DTI ratio. If the borrower qualifies, the old mortgage should be paid off and the principal amount bifurcated into a new 90 percent LTV first mortgage and a priority second lien mortgage. The priority second mortgage would be owned by the government, and repayable by the borrower from gain on future sale of the residence or upon future refinance of the mortgage.

MBA believes the first and second lien mortgages that result from the above should be held initially by the government if they cannot be sold immediately into the secondary market.



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