



First Look at Key Provisions in the Homeowner Affordability and Stability Plan Revised February 25, 2009

Overview: The “Homeowner Affordability and Stability Plan” seeks to help borrowers through one of or a combination of three initiatives: 1) Using Fannie Mae or Freddie Mac to refinance mortgages with loan to value ratios (LTVs) exceeding 80 percent and up to 105 percent; 2) Providing financial incentives to servicers and lenders who assist financially troubled borrowers modify their loans before they become delinquent; or 3) Allowing judicial modifications to mortgages during bankruptcy for borrowers as a last resort. Empowering judges to make such modifications to the loan would have to be authorized by Congress first.

Fannie Mae and Freddie Mac: The plan would enable borrowers who have conforming loans owned or guaranteed by Fannie Mae or Freddie Mac (GSE) to refinance through the agencies, even if the loans have LTVs higher than 80 percent but no greater than 105 percent. The charters of Fannie Mae and Freddie Mac prohibit them from owning or securitizing loans with LTVs greater than 80 percent without credit enhancements, such as mortgage insurance (MI). However, the Federal Housing Finance Agency (FHFA) issued a statement saying that the GSEs will not be required to expand existing MI or place new MI coverage for the new mortgage even if the LTV is higher than 80 percent. FHFA asserted that new or enhanced MI coverage is unnecessary because the GSEs already hold the credit risk of the mortgage. The plan also increases the federal backstop for the GSEs viability by providing an additional \$100 billion for each GSE (up to \$200 billion) under the Preferred Stock Purchase Agreements and increases the GSEs’ portfolio caps by \$50 billion to \$900 billion, along with corresponding increases in their allowable debt outstanding. Treasury estimates that this use of Fannie Mae and Freddie Mac will help four to five million borrowers.

Homeowner Stability Initiative: Under this aspect of the plan, Treasury will work with the GSEs, the Federal Housing Administration (FHA) and the Federal Deposit Insurance Corporation (FDIC) on several activities, discussed below, including modifications, incentives, compensation and guidelines for loan modifications. This initiative would also require that financial institutions receiving federal financial assistance to follow the government’s loan modification guidelines, and would authorize judges to modify mortgages in bankruptcy proceedings (cramdown). The initiative would strengthen FHA programs and provide support for local communities. The government would commit \$75 billion to this “Homeowner Stability Initiative” or HSI.

Modifications: HSI would reduce payments through a reduction in the interest rate or principal. To participate, a lender would be required to reduce the interest rate on the loan to achieve a 38 percent debt-to-income (DTI) ratio for the borrower, and then the federal government would share the cost of further interest reductions dollar-for-dollar with the lender to achieve a 31 percent DTI, either through interest rate or principal forgiveness. Lenders must keep the payment in place for five years, and after that time the interest rate may be stepped up to the loan rate in place at the time of modification.

Incentives and Servicer Compensation: HSI will provide incentives to mortgage lenders, servicers and borrowers. For example, after a lender modifies a mortgage to lower a borrower's payment to a 38 percent debt-to-income ratio (DTI), the government will share the cost of lowering the borrower's payments to 31 percent DTI. Mortgage servicers would be eligible to receive payments to offset their cost of modifying loans, such as \$1,000 up-front for making eligible modifications. Servicers would also receive fees monthly, up to \$1,000 per year as long as the borrower stays current. Servicers would be encouraged to reach out to at-risk borrowers before a borrower falls behind on his payments. If an at-risk loan is modified prior to a borrower falling behind, servicers would receive an additional \$500 and mortgage holders would receive \$1,500. Borrowers in the program would receive \$1,000 per year toward their principal, for up to five years as long as they remain current in their payments.

Insurance Fund: As a further incentive to lenders to modify mortgages, Treasury would establish a partial guarantee insurance fund of up to \$10 billion to protect lenders from declines in home prices in the event that they later foreclose on the loan.

Uniform Guidance: Treasury will establish uniform guidelines on mortgage loan modifications for all lenders/servicers that participate in the HSI. Fannie Mae and Freddie Mac also will use these guidelines on loans they own or guarantee and the administration will work with regulators and other federal and state agencies to implement these guidelines across the mortgage industry.

Oversight: Treasury will require strong oversight, mandatory reporting and quarterly meetings of Treasury, the FDIC, the Federal Reserve and HUD to monitor performance.

Bankruptcy Cramdown: Authorizes bankruptcy judges to modify mortgages under Fannie Mae and Freddie Mac's conforming loan limits. However, borrowers *must* ask the lender for a modification before seeking bankruptcy remedies. This provision would require a legislative change in the bankruptcy code. Under the proposal, the principal in excess of the property value would be deemed "unsecured indebtedness."

Community Assistance: Provides \$1.5 billion in relocation and other forms of assistance to renters displaced by foreclosure and \$2 billion in neighborhood stabilization funds.

FHA Improvements: The plan would ease restrictions in FHA programs including Hope for Homeowners including reducing fees paid, increasing flexibility for lenders to modify troubled loans, permit borrowers with higher debt loads to qualify and allow payments to servicers of existing loans.

Matters that Could be Improved Upon

Coverage: The plan does not appear to cover borrowers with LTVs greater than 105 percent. This is a particular concern in areas such as California, Florida, Arizona, and Nevada.

Nonconforming Loans/Private Label Securities: Another limiting factor of the plan is that it does not offer assistance to borrowers with jumbo mortgages or those whose mortgages are in private label securities. Also, the plan does not provide servicers with a sufficient safe harbor to avoid litigation from the investor or mortgage holder when the servicer is trying to help a borrower with a jumbo or non-agency mortgage.

Warehouse Lending: The plan does not address the diminished availability of warehouse lines of credit. Without these lines, many independent mortgage bankers will not have sufficient funds to assist borrowers.

Appraisal Requirements: It is not clear how the appraisal process will work under this plan. The administration may want to consider the impact of the Home Valuation Code of Conduct developed as part of a consent agreement between Fannie Mae, Freddie Mac, the Federal Housing Finance Agency and the New York Attorney General.

Bankruptcy Cramdown: MBA continues to oppose bankruptcy cramdown for any primary residence mortgage indebtedness.

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