FHA Loss Mitigation

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Overview

- The goal of this session is to give you a basic introduction to FHA and FHA loss mitigation.

- Please raise questions during the presentation.

- Also, you can always call me or email at ssharpe@nclc.org

HUD insures loans

- The Federal Housing Administration (FHA) is under the United States Department of Housing and Urban Development (HUD).

- FHA insures loans that private lenders generally make to low- to moderate-income homeowners.

- According to HUD’s website – “[FHA] is one of the largest insurers of mortgages in the world, insuring more than 46 million mortgages since its inception in 1934.”

HUD insures loans

- If the lender suffers a loss on a loan (for example, due to a foreclosure), the lender submits a claim to FHA to cover the loss.

- FHA has rules about when a lender can make a claim.

- FHA allows a lender to submit claim payments in some cases in advance of foreclosure
  - DASP
  - Partial Claim

Ginnie Mae

- The role of Ginnie Mae often comes up in cases.

- Ginnie Mae stands for the Government National Mortgage Association and it is a wholly government owned corporation within HUD.

Ginnie Mae

- From their website: “What Ginnie Mae does is guarantee investors the timely payment of principal and interest on MBS backed by federally insured or guaranteed loans — mainly loans insured by the Federal Housing Administration (FHA) or guaranteed by the Department of Veterans Affairs (VA).”

- Key point - the rules and regulations from FHA apply to FHA-insured loans held in Ginnie Mae pools.

HUD Loss Mitigation

- The statute and regulations for FHA loans anticipate that borrowers might fall behind and that there should be alternatives to foreclosure available if they do.

Loss mitigation legal structure

Look at 12 U.S.C. 1708(a)(7)

- "The operational goals for the Fund are—

(A) to minimize the default risk to the Fund and to homeowners . . . ; and

(B) **to meet the housing needs of the borrowers that the single family mortgage insurance program under this subchapter is designed to serve**."

Loss mitigation legal structure

- Required reading
  - 42 U.S.C. 1441 – Congressional declaration of national housing policy
  - 42 U.S.C. 1441a – National housing goals

Loss mitigation legal structure

- In fact, there is a specific statute for loans in default and loss mitigation –
- 12 U.S.C. § 1715u(a): "Upon default or imminent default, as defined by the Secretary of any mortgage insured under this subchapter, **mortgagees shall engage in loss mitigation actions for the purpose of providing an alternative to foreclosure** . . . as provided in regulations by the Secretary."

Loss mitigation legal structure

- The regulations specify steps lenders must take to avoid foreclosure.
- Note the reference to the regulations in the statute.

Loss mitigation legal structure

- The FHA regulations are the main topic of case law because they have been directly incorporated into the borrower's contracts. 24 C.F.R. §§ 203.500 - .681.

- The face-to-face meeting regulation, 24 C.F.R. § 203.604, gets the most publicity and the vast majority of case law treatment.

Loss mitigation legal structure

- Don’t forget about the other regulations, especially 24 C.F.R. § 203.605 regarding loss mitigation evaluations and language in 24 C.F.R. §§ 203.600, .602 & .606.

Loss mitigation legal structure

- Main document is HUD Handbook 4000.1, which provides the comprehensive guide to FHA mortgages
  - https://www.hud.gov/program_offices/housing/sfh/handbook_4000-1
- Mortgagee Letters
  - HUD updates policies through Mortgagee Letters that are added to Handbook 4000.1
- Form note and mortgage

Loss mitigation

- There are specific options for FHA-insured loans.

- It is important to note that HUD did not cancel its version of the Home Affordable Modification Program (HAMP)

- In fact, FHA-HAMP is the centerpiece of HUD’s program.

Loss mitigation

- We are covering the standard loss mitigation options.

- The COVID options will be covered later in the conference.

Loss mitigation

- Effective August 17, 2021, there is a new chart to use to determine the proper loss mitigation option for a borrower.

- It is now formatted as a list of yes/no questions.

Loss mitigation

- The Handbook text before and after the chart fills in important eligibility details.
- There are lots of little details that we discuss in the Mortgage Servicing chapter.
- For now though, we want to walk through how the option is selected.

Loss Mitigation Waterfall Options			
Question	**Decision Point**	**Yes**	**No**
1	Is the Borrower an Owner-Occupant?	Question 2	Informal or Formal Forbearance or Question 9
2	Has the Borrower experienced a verified loss of income or increase in living expenses?	Question 3	Informal or Formal Forbearance or Foreclosure
3	Is one or more Borrowers receiving Continuous Income?	Question 4	Special Forbearance-Unemployment
4	Can a Mortgage Payment at or below the target monthly Mortgage Payment be achieved by re-amortizing the total outstanding debt for 360 months at the Market Rate?	FHA-HAMP Standalone Loan Modification	Question 5
5	Is the Borrower's current interest rate at or below Market Rate, and is the current Mortgage Payment with re-analyzed escrow at or below the target payment?	FHA-HAMP Standalone Partial Claim	Question 6
6	Can the FHA-HAMP Combination Loan Modification and Partial Claim bring the loan current with a Mortgage Payment at or below 40% of current income?	FHA-HAMP Combination Loan Modification and Partial Claim	Question 7

Loss Mitigation Waterfall Options			
Question	**Decision Point**	**Yes**	**No**
7	Is the FHA-HAMP Combination Loan Modification and Partial Claim Mortgage Payment at or greater than 40% of current income, and one or more Borrowers are unemployed?	Special Forbearance-Unemployment	Question 8
8	Has the Borrower been determined ineligible for all Home Retention Options, but has income or other assets to repay the indebtedness within six months?	Formal Forbearance not to exceed six months	Question 9
9	Does the Borrower meet the requirements to participate in a Pre-Foreclosure Sale (PFS)?	Streamlined PFS or Standard PFS	Question 10
10	Does the total outstanding debt remain uncurable and was an attempt made to market the Property under the PFS Program?	Streamlined or Standard Deed-in-Lieu	Foreclosure

Loss mitigation

- We will walk through the initial questions and then use examples to illustrate how these actually work.
- The first three questions test if the borrower lives in the home, had a hardship, and has some income to evaluate.

Loss mitigation

- Question 1: Is the Borrower an Owner-Occupant?

- **Practice point**: The general rule is that FHA loss mitigation options are only available for owner-occupants.

- If yes, then question 2.

Loss mitigation

- Question 2: Has the Borrower experienced a verified loss of income or increase in living expenses?

- Practice point: FHA-HAMP is for clients who face a hardship. Take time in the interview to understand what happened and help them explain it. This can cause problems.

- If yes, then 3

Loss mitigation

- Question 3: Is one or more Borrowers receiving Continuous Income?

- Continuous income is defined broadly in the handbook.

- If there’s no stable income, then you look to a special forbearance when there has been a hardship.

Loss mitigation

- Basically, you need some form of income to do an evaluation
- If there is continuous income, move to question 4.

Loss mitigation

- Question 4: Can a **Mortgage Payment** at or below the **target monthly Mortgage Payment** be achieved by re-amortizing the total outstanding debt for 360 months at the **Market Rate**?

- This asks if a simple modification of the loan terms will lead to an affordable payment.

Loss mitigation

- Affordability is determined in reference to the “target monthly mortgage payment.”
- **It is a target.**
- It is not necessarily the mortgage payment the borrower will receive.

1. Calculate the target Mortgage Payment:
   A. Calculate 31% of gross income;
   B. Calculate 80% of current Mortgage Payment;
   C. Calculate 25% of gross income;
   D. Take the greater of B or C; and
   E. The lesser of A or D determines the target Mortgage Payment.

Loss mitigation

- To answer question 4, first determine the target payment

- Compare to the standalone modification, which requires:
  - Add arrears to the principal
  - Set the interest rate at the **market rate**
  - Extend the mortgage term to 360 months

Loss mitigation

- **Market rate**: “a rate that is no more than 25 bps greater than the most recent Freddie Mac Weekly Primary Mortgage Market Survey (PMMS) Rate for 30- year fixed rate conforming Mortgages (U.S. average), rounded to the nearest one-eighth of 1 percent (0.125 percent)…”

Loss mitigation

- If the modified payment hits the target, stop and the borrower receives the modification.

- If the modified payment is too high, then move to Step 5.

Loss mitigation

- Step 5: “Is the Borrower’s current interest rate at or below Market Rate, and is the current Mortgage Payment with re-analyzed escrow **at or below the target payment**?”

- Basically, this asks if the current loan terms would be fine.

Loss mitigation

- If yes, then standalone partial claim
- What is a partial claim?

Loss mitigation

- "A Partial Claim is FHA's reimbursement of a Mortgagee advancement of funds on behalf of the Borrower in an amount necessary to assist in reinstating the Delinquent Mortgage under the FHA-HAMP Option."

Loss mitigation

- A **standalone** partial claim simply brings the loan current.
- Borrower is not charged interest on the claim amount and does not make monthly payments on it.
- The borrower will have to pay later.

Example Problems

- Going to breakout rooms
- See if you can apply these

Loss mitigation

- If no to 5, then need a **combination modification and partial claim**

- The modification adjusts the interest rate and the term.

- The partial claim defers some of the amounts owed.

Loss mitigation

- Question 6: “Can the FHA-HAMP Combination Loan Modification and Partial Claim bring the loan current with a Mortgage Payment **at or below 40% of current income**?”

Loss mitigation

- This is a complicated question. Let’s break it down.

- Can you get a payment at or below 40% of the borrower’s income?

- That’s the ultimate eligibility question. It gets obscured in the back and forth between the servicer, but it is the ultimate rule.

Loss mitigation

- 40% is not the goal. You instead try to hit the target payment.
- You get only the amount of partial claim you need to reach the target.

Loss mitigation

- Let’s take an example to illustrate this.
- We’ll build off Problem 1, but change one fact.
- Let’s say Hal Homeowner makes $2,200 instead of $3,000.
- Hal is making less money and needs more payment relief.

Target

- The target payment will be lower than the original example.
  - $2200 x .31 = $682
  - .8 x $800 = $640
  - $2200 x .25 = $550

- The target here is $640/month, which is $392.20 (because escrow in this example is still $247.80

Loss mitigation

- We know the standalone modification will not work here.
  - It still generates a payment of $690.77 ($442.97 principal and interest)

- We also know that the standalone partial claim will not work here because the current payment ($800) is much higher than the target payment of $640.

Loss mitigation

- We know what the interest rate will be (3.75%, which is the market rate).
- We know what the loan term will be – 360 months.
- We know what our principal and interest payment target is - $392.20.

Loss mitigation

- We need to calculate what the balance should be to fit the other numbers.
- For this, we need a good calculator.
- At 3.75% annual interest, you can pay balance of **$84,687.28** with $392.20/month payments over 360 months.

Loss mitigation

- But we have to resolve a balance of $95,649.73?

- This is where we get a combination of the modification and the partial claim.

- The lender can use the partial claim to bring down the balance.

Loss mitigation

- There is a maximum partial claim, however, under the statute.

- You cannot, for example, drive the payment down to $1/month by giving $95,000 partial claim.

Loss mitigation

- The general rule is that the maximum partial claim is 30% of the loan balance at the time of default.
  - It gets more complicated to calculate if there are previous partial claims.
- Here the balance is $92,149.73
  - $92,149.73 x .3 = $27,644.919
- That's the **maximum** partial claim (not the partial claim the client receives).

Loss mitigation

- In this case, the client needs a partial claim of **$10,782.45** ($95,649.73 (balance plus arrears) - $84,687.28 (target balance)).

- **This partial claim is below the maximum.**

Loss mitigation

- What does the client get?
- $640/month ($392.20/month principal and interest) payment
  - 3.75% interest, 360 month term, $84,687.28 balance
- And a partial claim to HUD at 0% interest and $0/month payments of $10,782.45.

Loss mitigation

- If no back to forbearance possibilities and non-retention options.
- We aren't going to cover those but you may need them depending on case selection.

Remember

- There are statutes and regulations that apply for FHA insured loans.

- Keep Handbook 4000.1 handy.

- Email me or call if you have questions.

Questions?

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