

An Overview of Congressional and Administration Actions to Respond to the Subprime Mortgage Crisis

I. Legislative Actions

A. Mortgage Tax Relief Bill Signed into Law

On December 20, President Bush signed into law a mortgage relief tax bill which will provide a three-year exclusion from income of debt forgiven when a mortgage is foreclosed or renegotiated. The measure also offers a three-year extension of the private mortgage insurance deduction.

B. House Passes Mortgage Reform and Anti-Predatory Act

On November 15, by a vote of 291- 127, the House passed the Mortgage Reform and Anti-Predatory Lending Act that would

- Set standards for originating and securitizing subprime mortgages,
- Expand the definition of high-cost loans under the Home Ownership and Equity Protection Act of 1994 (HOEPA) to include first-lien mortgages more than 8 percentage points over a benchmark Treasury security, second-liens mortgages over 10 percentage points, and mortgages including total points and fees of more than 5 percent of the loan amount;
- Place new restrictions on these "high-cost" mortgages;
- Expand legal options for borrowers;
- Impose new rules for appraisers;
- Preempt states from imposing tougher rules in regard to standards set for the secondary market, but would leave room for states to set a higher bar for consumer protections in regard to loan originators; and
- Impose assignee liability at the securitizer, who bundles mortgages and sells mortgage-backed securities, while offering investors a "safe harbor" if they purchase mortgages that meet certain standards of quality.

C. Chairman Dodd Introduces Predatory Lending Legislation

On December 12, Senate Banking Committee Chairman Christopher Dodd (D-CT) introduced legislation stronger than the House-passed legislation. As introduced, the bill includes

- A complete ban on prepayment penalties, yield spread premiums and debt-to-income ratios above 45% for subprime and nontraditional mortgages;
- An expansion of the definition of "high-cost" loans;
- Suitability standards;

- Delays to the foreclosure process;
- No federal preemption of state law; and
- No assignee liability safe harbor for investors.

It is generally known that Chairman Dodd has introduced this legislation as a starting point and that any legislation that might be reported out of the Senate Banking Committee and later passes the Senate will be dramatically different.

D. Bankruptcy Reform under Consideration

On December 12, the House Judiciary Committee approved a bill that would let bankruptcy judges modify subprime and nontraditional mortgages made from Jan. 1, 2000, through the bill's enactment date with a sunset in seven years. Senate Majority Whip Richard Durbin (D-IL) is pursuing his own somewhat broader bill and trying to reach a deal with Sen. Arlen Specter (R-PA), the Senate Judiciary Committee's lead Republican.

E. FHA Mortgage Reform Bills Pass House and Senate

The House (349-72) and Senate (93-1) have both passed FHA Reform legislation in 2007. The bills are now in a House-Senate conference which must iron out differences before the bill goes to the President for signature.

Both bills increase the maximum mortgage that can be insured by the FHA. The Senate bill raises the maximum high-cost areas from \$362,790 to \$417,000 (the same as the conforming loan limit for Fannie Mae and Freddie Mac) while the House bill increases the amount to \$729,750 in high-cost areas.

The Senate bill lowers the current 3 percent FHA down payment requirement to 1.5 percent, while the House allows no-down payment mortgages.

Low-priced areas in both bills would be raised to \$271,050 from \$200,160.

The House bill extends the maximum term of the mortgage to 40 years from 35, while the Senate bill makes no such change.

F. Administration Backs Expansion of Tax-Exempt Mortgage Bonds

Under current law, state and local housing agencies are allowed to issue tax-free bonds only to help subsidize the cost of mortgages for first-time home buyers or home buyers purchasing property in distressed areas. The Administration is proposing that the law be amended to allow refinancing for subprime borrowers.

In addition, Treasury officials have supported increasing the dollar cap on the amount of tax-free bonds issued by states and localities by \$15 billion over three years.

II. Regulatory Action – The Fed’s Proposed Mortgage Lender regulation

On December 18, the Federal Reserve Board issued for comment a proposed rule that would increase regulation of mortgage lenders, including those currently unregulated. The amendment to Regulation Z (Truth in Lending), which implements HOEPA addresses a wide range of abuses.

- "Higher-priced" loans must be underwritten on the basis of the borrower's ability to repay, rather than a residential property's collateral value. Higher-priced loans are defined as any first-lien mortgage with an interest rate of 3 percentage points over a Treasury security of comparable maturity which is identical to the definition for higher-priced mortgages under the Home Mortgage Disclosure Act (HMDA). The threshold for second liens would be 5 percentage points.
- Lenders that exhibit a "pattern or practice" that violates such standards could be subject to civil liability under the proposal.
- Lenders must take reasonable measures to verify borrowers' income and assets and require establishment of escrows to assure tax and insurance costs are folded into consumers' monthly payments.
- Prepayment penalties are limited but not prohibited under all circumstances.
- Lenders' payments to mortgage brokers are limited, unless the borrower receives appropriate and timely disclosures. Yield spread premiums are prohibited unless the broker signs a written agreement with the borrower that discloses the total dollar amount of the compensation due to the broker.

Senate Banking Committee Chairman Christopher Dodd (D-CT) and House Financial Services Committee Chairman Barney Frank (D-MA) both criticized the rule in very strong terms as not going far enough.

III. Government-Private Sector Initiative – The Hope Now Program

Excerpts from Treasury and White House material describing the Hope Now program for subprime mortgage relief program:

The Hope Now Alliance consists of four counseling organizations, 21 mortgage servicers and lenders (comprising 65 percent of the U.S. market for mortgage servicing and almost 85 percent of the subprime servicing market), three investor groups (including the American Securitization Forum, which represents over 370 members), and 10 trade associations. This is a private sector effort, involving no government money

Hope Now members have agreed on a set of new industry-wide standards to provide systematic relief to these borrowers in one of three ways: refinancing an existing loan into a new private mortgage; moving them into an FHA loan; or freezing their current interest rates for five years.

The current system for working out problem loans would not be sufficient to handle the anticipated 1.8 million owner-occupied subprime mortgage resets that will occur in 2008

and 2009. 50 percent of foreclosures occur without borrowers ever talking to their lender or a mortgage counselor. In the past, some servicers may not have contacted borrowers until after their loans were delinquent. Today, all Hope Now servicers are contacting borrowers 120 days in advance of their mortgage reset, to reach them early, before their mortgage problems become overwhelming.

The standard loan-by-loan evaluation process that is current industry practice would not be able to handle the volume of work that will be required. To deal with this, the Hope Now alliance is developing

- New industry guidelines, to be issued by the American Securitization Forum, to create an efficient process for identifying borrowers who qualify for a loan modification or refinancing. Under this new agreement, the servicers estimate that up to 1.2 million subprime, adjustable rate mortgage holders may be eligible for a fast-track refinance or loan modification
- Standard measures which will identify categories of borrowers who can be helped, determine successful treatments, and measure the rate of successful outcomes.
- Developing an approach based on four levels of sub-prime borrowers:
 1. Those who can afford their adjusted interest rate, these homeowners need no assistance.
 2. Homeowners who haven't been making payments at the starter rate on their sub-prime loan, and may not have the wherewithal to sustain home ownership. These homeowners will likely become renters again.
 3. Homeowners might choose to refinance their mortgage, putting them in a sustainable mortgage while keeping investors whole. This is the first, best option. Servicers should move quickly to assist those who can refinance.
 4. Those with steady incomes, and relatively clean payment histories who could afford the lower, introductory mortgage rate, but cannot afford the higher, adjusted rate. We are focusing on this group, determining who they are and what steps may be appropriately taken to assist them.