National Consumer Law Center

NATIONAL HEADQUARTERS
7 Winthrop Square, Boston, MA 02110
(617) 542-8010

WASHINGTON OFFICE
Spanogle Institute for Consumer Advocacy
1001 Connecticut Avenue, NW, Suite 510
Washington, DC 20036
(202) 452-6252

NCLC.ORG

August 27, 2021

Sandra L. Thompson
Acting Director
Federal Housing Finance Agency
400 7th Street, SW
Washington, D.C. 20219

Dear Acting Director Thompson:

On behalf of the clients and communities we represent, we urge the Government Sponsored Enterprises (GSEs) to amend the COVID-19 payment deferral and Flex Modification for COVID-19 impacted borrowers to allow deferral and capitalization of escrow shortages. We appreciate that the GSEs have provided comprehensive forbearance and post-forbearance options for borrowers who have suffered a COVID-19 hardship. It is essential, however, that the GSEs take further steps to ensure that these important programs provide consistent, affordable payments that borrowers can sustain and not increase borrowers' monthly payments to a level they can no longer afford due to an escrow shortage. Specifically, the GSEs should 1) require servicers to perform an escrow analysis before placing a borrower in a COVID-19 payment deferral plan, as is required under the Flex Modification program, and 2) require any resulting shortage to be placed in the deferred balance at the end of the loan or capitalized with a Flex Modification.

We Know from the Great Recession that Escrow Shortages are a Problem

We have seen first-hand from the GSE HAMP modifications that took place during the Great Recession how a failure to capitalize escrow shortages can derail a borrower's monthly payments and put them on the path to foreclosure. During HAMP, past due interest and escrow advances were capitalized into the unpaid principal balance of the loan. At that time, an escrow analysis was not required before the loan was modified. It could be months after the loan was modified that the annual escrow analysis was performed, at which point a borrower would be hit with an additional payment each month to make up the shortage. This put many borrowers at risk of re-default because they could not make the increased payment.

The main purpose of the COVID-19 payment deferral plan is to allow borrowers to resume their pre-COVID payments. One of the first questions a servicer will now ask is whether the borrower can afford to make their regular monthly payments again. A borrower who answers in the affirmative is unlikely to realize that this payment can and most likely will increase shortly because of an unknown escrow shortage payment. Even if the servicer offers a repayment plan of up to 60 months to catch up on an escrow shortage, that is not enough for some borrowers. Likewise, borrowers who need and receive more relief in the form of a Flex Modification will experience payment shock if they initially are provided an affordable modified payment and then are sent a statement with a monthly increase for a shortage.

While many borrowers have transitioned successfully from forbearance to post-forbearance plans, those who remain in forbearance plans are those that need the most help. They are typically borrowers of color, who have been disproportionately harmed by the pandemic. They may have lower credit scores and live in lower-income neighborhoods, putting them at greater risk of foreclosure when the forbearance plans end. Even a $25 extra payment each month could cause them to re-default on their mortgage.

COVID-19 Relief Options for Borrowers Should be Consistent

The foreclosure stays and widespread implementation of forbearances that began in April 2020 created the unprecedented situation where, through 2021, we have seen the lowest rate of foreclosure starts recorded at any time since 1982.[1] At the same time, the number and rate of mortgages in seriously delinquent status equals what we saw during 2010-11. Given these unique circumstances, it is more important than ever to create consistent, simple terms for post-forbearance relief for borrowers.

With the majority of forbearance plans ending over the next four months, it is vital that the GSEs align with FHA to eliminate confusion and misunderstanding of options for both servicers and borrowers. Based on estimates, servicers may have to process up to 18,000 expiring plans per business day in September and October alone.[2]

Consistency of the escrow terms in the COVID-19 options offered by the GSEs and FHA, who together make up the majority of the mortgage market, is one key way to help provide a smooth transition for borrowers coming off forbearance plans. The GSEs programs should align with HUD's FHA COVID Recovery options, which require servicers to place escrow shortages in a partial claim at the end of the loan or capitalize them into a modified loan. The GSEs should likewise require servicers to place escrow shortages in a deferred balance with the COVID-19 payment deferral plan or capitalize the shortage into the unpaid principal balance in a Flex Modification.

In its 2021 Mortgage Servicing COVID-19 Final Rule, the CFPB clarified that section 1024.17 of Regulation X "does not prohibit the borrower and servicer from agreeing to a loss mitigation option that allows for the repayment of funds that a servicer has advanced or will advance to cover an escrow shortage." (86 Fed. Reg. 34848, 34871) The GSEs could allow a shortage to be placed in a deferred balance or capitalized into the loan during a modification and such an agreement would not violate Regulation X. The CFPB also stated that it "strongly encourages" servicers to conduct a short-year escrow analysis in connection with a loss mitigation review, noting that "[d]oing so may help avoid unexpected potential escrow related payment increases

[1] Mortgage Bankers Ass'n National Delinquency Survey First Quarter 2021, p. 2
[2] Black Knight Mortgage Monitor Report June 2021 p. 13.

after the borrower has already agreed to a loss mitigation option….” (86 Fed. Reg. 34848, 34866).

The GSEs Need to Move Quickly- Problems are Already Surfacing

Housing counselors and advocates are already seeing issues with escrow accounts with post-forbearance options.

One borrower’s experience provides an excellent example of why the GSEs should create simple terms for dealing with the escrow account: require an escrow analysis and defer or capitalize both the advances and shortages. This borrower in Massachusetts has a Freddie Mac loan that was in forbearance for 15 months. He was approved for a COVID-19 deferral payment plan and was set to resume his monthly payment of principal and interest in the amount of $798 on July 1, 2021. The pre-pandemic escrow payment was $376.42 for a total PITI of $1,174.42. The servicer informed the borrower that there would be an increase in the escrow payment, however. The servicer stated it had paid the tax bills since April 2020 and there was a negative amount of $4,670.00 in the account that needed to be repaid over 24 to 36 months. This would equate to an increase in payment of $194.58 or $129.72 per month, depending on the length of the repayment plan. The borrower lives on a fixed income and can just afford the pre-pandemic payment. Even with a 60-month repayment option, he would have to pay an additional $77.83 per month. Through working with a housing counselor, the borrower also realized that his escrow payment going forward would increase due to an increase in real estate taxes. These increases together would mean that the loan would become unaffordable.

First, this example highlights the confusion servicers are having with determining which amounts can and cannot be deferred. Escrow advances, such as the amounts the servicer paid in real estate taxes in the past year, should be deferred. Freddie Mac Bulletin, 2020-15, 4 (May 13, 2020) (“[a]ny Escrow advances must be included in the deferred balance.”). Requiring an escrow analysis to be performed before a deferral plan is implemented would provide servicers with the correct information about both advances and shortages. Allowing both advances and shortages to then be included in the deferred or capitalized balance would eliminate any confusion regarding their treatment and provide a simple, easy way for servicers to deal with escrow balances.

Next, the servicer here is telling the borrower he has to repay those amounts now over 24 to 36 months. If some portion of the amount demanded by the servicer as an additional escrow payment was in fact an escrow shortage, under the Freddie Mac Guide, 9206.15, the servicer can offer a repayment plan as low as 12 months or *up to* 60 months. Because of the extraordinary relief that borrowers have needed during the COVID-19 pandemic of missing 12 to18 months of payments, it is likely many will not be able to afford the resulting escrow shortage payment on top of their regular mortgage payment, even if it is spread over 60 months. Allowing shortages to be deferred or capitalized would eliminate this problem and minimize the risk of borrowers re-defaulting on their loans.

We are hearing similar stories from housing advocates across the country that borrowers are either being told incorrectly that they have to repay amounts that have been advanced by the servicer or, shortly after they enter into a deferral or Flex modification, they are surprised with an increase in their monthly payment due to an escrow shortage.

An escrow analysis is already required before a Trial Plan is provided for a Flex Modification. The same requirement could easily be put in place for the COVID-19 deferred payment plan. If the shortage can be deferred or capitalized, the borrower may have a fighting chance of being able to sustain their pre-forbearance payments. Borrowers will also have the information they need to determine whether they should accept a deferral plan or request to be reviewed for a Flex Modification to help offset an increase in their taxes and/or insurance.

As economic uncertainty continues and the majority of borrowers begin to come off their forbearance plans, the GSEs need to act swiftly to ensure that servicers have easy-to-implement, consistent post-forbearance solutions to offer to borrowers. The GSEs should require servicers to perform an escrow analysis not only before offering a Trial Plan for a Flex Modification but also before implementing a COVID-19 deferred payment program. The GSEs should also require both escrow advances and shortages to be deferred and/or capitalized. We urge the FHFA to direct Fannie Mae and Freddie Mac to implement these changes no later than September 30, 2021 due to the surge of borrowers exiting forbearance plans in the next four months.

For further discussion, please contact Andrea Bopp Stark, staff attorney with the National Consumer Law Center at astark@NCLC.org**.**

We thank you for your commitment to helping homeowners during the COVID-19 pandemic and for your attention to this recommendation.

Sincerely,

National Consumer Law Center (on behalf of its low income-clients)

Americans for Financial Reform Education Fund

Center for Responsible Lending

Community Legal Services of Philadelphia

Consumer Action

Consumer Federation of America

Greater Boston Legal Services, on behalf of its low-income clients

Jacksonville Area Legal Aid

Legal Aid Society of Southwest Ohio, LLC

Legal Aid Society of the District of Columbia

Legal Services Center of Harvard Law School

Maine Equal Justice

National Fair Housing Alliance

National Housing Law Project

National Housing Resource Center

Woodstock Institute