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US - Financial Services, 2010 Segment Trends

Short Sales

Mortgage Banking / Servicing : Short Sales becoming more popular

Briefing paper on increasing Short Sale pipelines

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What is a Short Sale?

Simply put, this is a real estate sale transaction where the Borrower owes more to the Lender/ investor than what the market value is for the same property. This is commonly known as being upside down or under water. When a Short Sale is approved it means that the Lender/ Investor is willing to accept less than the UPB (unpaid principal balance) as full payoff of the loan. Only the lien holder and mortgage insurer can approve Short Sales.

If the loan was originated with PMI (private mortgage insurance), the insuring company will receive a claim from the loan servicer for a % of the loss the lien holder will incur from the Short Sale. If the loan was not originated with PMI (with 20% down payment or more), the full loss of the Short Sale will be absorbed by the Lender/ Investor and a Deficiency Promissory Note or Deficiency Judgment Letter may be asked of the Borrower for the difference.

Many states prohibit the deficiency practice on owner occupied purchases and refinances, but where permitted, Borrowers often include this debt into a subsequent Bankruptcy. It's also important to note that there are tax consequences (1099) for borrowers that benefit from such debt relief.

It appears that...

Until modifications start implementing principal reductions across the board, many Homeowners will opt for foreclosure and renting a cheaper home, than retaining a property that keeps losing value with every new foreclosure that hits the market. These mindsets together with the high % of Homeowners who don't qualify for a loan modification are increasing the servicers' pipeline of the next best loss mitigation option, the Short Sale. This growing trend is stretching the servicer shop's capacity to process loss mitigation in a timely manner.

A decade ago few people on main street had heard of a Short Sale. Today, Homeowners, real estate agents, regulators and pool investors alike have knowledge and express feelings about this transaction type. Short Sales are growing in popularity as an exit strategy for distressed homeowners of upside down properties but, because they have to be approved by all lien holders and PMI companies, these transactions often get lost in a servicer's slow response and less than eager negotiators that face delegation limits (typically maxed out at 80% of the property value), data from 3rd parties and strict loss mitigation guidelines.

Short Sale purchase contracts have a short shelf life since the prospective buyer may lose interest over time and all hardship validating documents required by the investor guidelines from the seller must be updated within 60 days of submission. Many Short Sales are lost in work queues before final approval is secured, thereby, sending the seller to start the frustrating Short Sale process all over again.

The Lender/ Investor/ Mortgage Insurer also experience extreme frustration as they see NPL (non performing loans) portfolios continue to deteriorate and real estate properties loose incremental value as more foreclosures are executed, thereby, adversely affecting appraisals and comparables. To complicate matters, the outcome of every loss mitigation transaction depends on the ability, agility and rules based systems of mortgage servicers whose efficiency may not support the loss mitigation process due to the sheer volume of defaulting loans.

The US Treasury is aware of the Homeowner and Investor frustrations and on April 5, 2010 will roll out

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the HAFA (Home Affordable Foreclosure Alternatives) Short Sale and DIL (Deed in Lieu) requirements in an effort to discourage foreclosures. Like the HAMP (Home Affordable Modification Program), the HAFA Short Sale offers incentives that could cost the Treasury up to \$3500 per transaction in incentives to Homeowners, Investors and Servicers.

HAFA will allow Homeowners to receive a pre-approval from their Servicer prior to listing the property for sale, as well as a relocation incentive of \$1500 after closing. Investors will get \$1000 for approving up to \$3000 to go to subordinate lien holders from the Short Sale proceeds. Servicers too will receive an incentive to cover administrative cost of \$1000 per transaction. Servicers are allowed to implement this new program prior to the roll out date, provided they signed up for HAMP / HAFA before December 31, 2009.

A growing challenge for mortgage servicers...

The mortgage servicer is charged with minimizing the losses of the Lender / Investor while at the same time educating distressed homeowners and real estate agents into a debt relief solution that meets Treasury/ Lender/ Investor/ Mortgage Insurer guidelines in a short time frame and with a multitude of operating systems struggling to keep up with the rule changes published by regulators. With the announcement of HAFA the Short Sale pipelines are swelling in servicers' shops across the country.

Going forward, Servicers will need to evaluate a borrower for a HAMP modification prior to any consideration being given to HAFA options in accordance with the provisions of Supplemental Directive 09-01 and any supplemental HAMP guidance. Borrowers that meet the eligibility criteria for HAMP, but who are not offered a Trial Period Plan, do not successfully complete a Trial Period Plan, or default on a HAMP modification should first be considered for other loan modifications or retention programs offered by the Servicer prior to being evaluated for HAFA.

In accordance with the provisions of Supplemental Directive 09-01 requirements - a delinquent loan meets the basic eligibility criteria, if all of the following conditions are met:

- The property is the Borrower's principal residence;
- The mortgage loan is a first lien mortgage originated on or before January 1, 2009;
- The mortgage is delinquent or default is reasonably foreseeable;
- The current unpaid principal balance is equal to or less than \$729,7501; and
- The Borrower's total monthly mortgage payment (per sd09-01) exceeds 31% gross

Pursuant to the servicer's policy, every potentially eligible Borrower must be considered. An amazing fact is that with all servicers have to consider, calculate and implement into their workflows, some Servicers are reviewing and processing loss mitigation transactions manually. Insane right? Yet true!

How to make it better?

Mortgage default executives and portfolio managers in servicing shops with capacity, processing and/or technology issues would benefit from unbiased external consulting services that will validate what they are doing well, map current conditions of process workflows, describe performance gaps, and identify what could be done better, faster and cheaper, by developing a customized Roadmap.

iGlass Consulting achieves this by designing a Roadmap as a master plan with detailed recommendations that can aid in reaching desired targets through initiatives such as:

- Customer self service options
- Paperless documentation solutions
- Staff utilization and flexible schedules
- Knowledge and compliance solutions
- Delegation criteria for non GSE loans
- Agile and comprehensive loss mitigation decisioning
- Simplified process workflows

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- Interaction with 3rd party vendors
- Systems integration options
- Shorter transaction cycle times
- Quality controls for customer satisfaction
- Effective customer contact options
- Additional capacity options
- Sustainable production goals
- Flexible report creation
- Measurable success

iGlass Consulting can be the catalyst that servicers need to achieve greater loss mitigation success. Our company provides over 80 years of combined achievements in management consulting with proven methodologies and tools that help our clients get on track for;

- Improved portfolio performance
- HAMP/ HAFA incentives
- Enhanced production
- Increased revenue
- Growth

Resulting in...

Enhanced effectiveness of tactics to defend the institution's financial assets.

Contributing sources...

<http://www.treasury.gov/> - <http://www.makinghomeaffordable.gov/>
<https://www.efanniemae.com/home/index.jsp> - <http://www.freddiemac.com/sell/guide/>
https://www.hmpadmin.com/portal/programs/foreclosure_alternatives.html
plus... HousingWire.com – DSNews.com – Mortgage Servicing News - MBA