**Policy 7625: Residential Real Estate Loss Mitigation Strategies**

**Model Policy Revised Date: 05/13/2024**

**General Policy Statement:**

Where economically feasible or appropriate, [[CUname]] (Credit Union) will work constructively with residential borrowers who are financially unable to make their contractual payment obligations on their home loans, consistent with safe and sound lending practices. This policy outlines the factors that the Credit Union will take into consideration when deciding whether to modify a residential loan, and the options when a loan modification would not effectively mitigate a loss.

1. **RISK ASSESSMENT AND STRATEGIC PLANNING**. The Credit Union will identify “at risk” loans before payment performance issues emerge. At a minimum, the risk assessment and strategic planning will consider the following:

	1. The number and volume of adjustable-rate mortgage loans that are at risk of default because of impending resets, including junior lien equity loans with subordinate lien positions to senior adjustable-rate mortgages;
	2. The number and volume of mortgage loans that are stated income, brokered, and/or non-traditional (e.g., interest only payments), as these types of loans are of higher risk than traditional mortgage loans;
	3. The number and volume of mortgage loans that exceed the current fair market value of the property, and anticipated value over the next 12-24 months, and an estimate of the Credit Union’s total loss exposure (difference between the loan balance and fair value) in relation to net worth;
	4. The impact of foreclosures versus any proposed loan modification on the financial performance of the Credit Union (earnings, net worth, asset liability management (ALM) model results, liquidity, etc.), ensuring management strategy provides for sufficient cash flow to meet operational and lending needs and the least expense to the Credit Union; and
	5. Other foreclosure prevention options if borrowers do not qualify for a loan modification.
2. **RESPONSIBILITY**. The [[7625-1]] is responsible for approving all mortgage loan modifications. The recommendation and approval process will be kept completely separate.
3. **MORTGAGE SERVICING REQUIREMENTS**. The Credit Union will follow all requirements of the Mortgage Servicing Rules published by the Consumer Financial Protection Bureau (CFPB) and the requirements, as they apply to the Credit Union, and the guidelines of the Credit Union’s Mortgage Servicing Policy.
4. **ELIGIBILITY REQUIREMENTS.** Before modifying a residential loan, the Credit Union will take the following factors into consideration:

	1. **The Condition of the Borrower(s).**

		1. The ability to repay a modified loan under a workout arrangement, including a review of current credit reports and income verification.
		2. Whether the inability to repay the loan under the current terms is temporary or long-term.
		3. Whether there is a guarantor.
	2. **The Condition of the Loan.**

		1. The amount delinquent.
		2. The length of time the loan is past due.
		3. Whether the loan documents are in order (i.e., signed, recorded, and contain all of the correct information).
	3. **The Condition of the Property.**

		1. Determine current property value.
		2. Whether there is property damage that would significantly affect its value (i.e., damage due to fire, flood, wind, or other natural disaster; environmental contamination, etc.).
		3. Whether there has been a significant change in the area surrounding the property that would affect its value (i.e., high number of foreclosures, zoning changes, or physical or environmental damage to surrounding area).
	4. **The Condition of the Title.**

		1. Whether the Credit Union remains in first lien position through an updated title search.
		2. Whether there have been conveyances (i.e., deeds).
		3. Whether there are any junior liens.
		4. Whether there are any delinquent tax and/or mechanics liens on record.
		5. Whether there are any *lis pendens* (suit pending) on record.
5. **DOCUMENTATION**. The Credit Union will document the reason(s) for the mitigation strategy (e.g., hardship letter) and, if it is a modified loan, the borrower’s commitment to pay. This documentation will be kept in the loan file.
6. **TYPES OF LOSS MITIGATION STRATEGIES.**

	1. **Refinancing.** The Credit Union may choose to refinance a loan if the borrower has sufficient equity and the ability to pay a more affordable mortgage.
	2. **Forbearance Plans.**The Credit Union may choose to temporarily agree to reduce or suspend payments for a short time to enable a borrower to catch up on missed payments or sell the home. The borrower must have some equity in the home, and the borrower’s financial issues must be temporary.
	3. **Loan Modifications.** When a borrower has little or no equity and the inability to pay the current loan payment, but desires to remain in the home, the Credit Union may choose to modify the loan.

		1. **Types of Loan Modifications**. The following types of loan modifications may be considered:

			1. Extending the term of the mortgage to reduce the monthly payment amount.
			2. Reducing the interest rate to lower the monthly payment amount;
			3. Changing from an adjustable rate to a fixed rate interest loan to eliminate payment shock;
			4. Rolling over past-due amounts and re-amortizing the new amount due;
			5. Forgiving past due amounts;
			6. Forgiving past due amounts and requiring a share of the equity in a future sale;
			7. Any other type of prudent, creative solution that does not violate safety and soundness.
		2. **Legal Review**. Before implementing a loan modification program, the Credit Union will consult with its attorney (who is versed in real estate law) to ensure that all of the loan modification documents conform to state law requirements (e.g., state real estate, lien, consumer protection, and Federal Trade Commission laws and regulations), as well as the applicable NCUA, state regulations and consumer protection laws (e.g., Truth-in-Lending, Equal Credit Opportunity, Fair Lending, Real Estate Settlement Procedures Act, etc.). The Credit Union will also request the legal review to address state laws applicable to foreclosure and other debt collection options.
		3. **Underwriting**. The Credit Union will follow its underwriting standards including the ability to repay requirements and at a minimum, the following:

			1. A credible analysis of the borrower’s capacity to repay the loan according to its modified terms (i.e., verification of gross monthly income for all borrowers who have signed the note (e.g., last year’s tax returns, recent pay stubs, etc.)).
			2. A current credit report for each borrower, or a joint report for a married couple, to validate monthly installment debt, revolving debt, and secondary mortgage debt.
			3. A target affordable housing-to-gross income (HTI) ratio and total debt-to-income (DTI) ratio.
			4. Estimate the cost to the credit union, as measured by a net present value (NPV) test, of any approved modification to verify it is less than the estimated cost of foreclosure or other foreclosure prevention alternative (e.g., short sale, deed in lieu of foreclosure, cash for keys, etc.), unless extenuating circumstances exist, and document the NPV analysis in the loan file.
		4. **Cash Advances/Releases of New Money**. Cash advances and releases of new money as part of a loan modification will be prohibited, except for settlement of delinquent real estate taxes, insurance and other amounts that protect the Credit Union’s collateral position.
		5. **Limitations**. The Credit Union will only agree to modify a loan [[7625-2]] before proceeding to a short sale, deed in lieu of foreclosure, or foreclosure.
		6. **Monitoring And Reporting**. The Credit Union will monitor and provide monthly reports to the Board on modified real estate loans. These reports will track the following:

			1. The number and volume of each type of modified loan;
			2. Delinquency and charge-offs;
			3. First payment defaults;
			4. Principal reductions;
			5. High loan-to-value (LTV) ratios, particularly in areas with continued market declines, and total loss exposure in relation to net worth;
			6. High DTI ratios;
			7. Credit quality; and
			8. Number of times a loan has been modified.
		7. **Accounting and Allowance for Credit Losses (ACL)**. The Credit Union will comply with the general loan workouts, modifications and nonaccrual standards policy and corresponding accounting treatment.
	4. **Pre-Foreclosure Short Sale.** If the borrower has long-term financial problems and cannot afford even a modified loan, and the value of the property has fallen below the mortgage amount, the Credit Union may choose to release its mortgage and sell the home for less than the outstanding loan amount. In these situations, the Credit Union takes one hundred percent (100%) of the sale proceeds.

		1. **Deficiencies.** The Credit Union will need to decide whether to release the borrower from any deficiency after the sale.
	5. **Deed in Lieu of Foreclosure.** The Credit Union may choose to accept a deed from borrower signing over title to the property in exchange for being released from their debt. The Credit Union will first obtain an appraisal to determine whether the current value makes this an attractive option and will seek the advice of legal counsel to ensure that the transaction, as well as the documentation, is conducted properly. The mortgage discharge will not be filed until the property is sold.
	6. **Foreclosure.** As a last resort, the Credit Union will begin the process of foreclosing on the property. In doing so, the Credit Union will follow the state foreclosure law, or obtain legal counsel to do so.
7. **LOAN MODIFICATION DENIALS.** The Credit Union may determine that the member is not eligible for a loan modification or payment deferral. The Credit Union will follow their procedures for providing adverse action notice as required by the applicable regulation (Regulation V which implements the Fair Credit Reporting Act or Regulation B which implements the Equal Credit Opportunity Act), depending on what information was used to determine the denial.

	1. Regulation B would not require an adverse action notice for denials of requests for loan modifications when the accounts are delinquent and in default. As a best practice, the Credit Union will still provide written notice to the member communicating the denial.
	2. Regulation V would require an adverse action notice when adverse action is taken based in whole or in part on any information in the consumer report (see Policy 11005 – Adverse Action Requirements).
8. **TAX IMPLICATIONS**. Some loss mitigation strategies may involve a reduction or forgiveness of principal that may result in additional tax liabilities for the borrower(s). The Credit Union will consult with its independent accountant regarding applicable IRS reporting requirements. The Credit Union will also encourage borrowers to consult with a tax advisor regarding the tax implications of principal forgiveness before an agreement is completed.