Fields of Opportunities

STATE OF IOWA

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Iowa Division of Credit Unions
Regulatory Advisory Bulletin

Loss-Mitigation for Real Estate secured loans:

This guidance is subject to change. Credit unions must complete their own due diligence for each of these compliance areas.

Background: The Iowa Division of Credit Unions has previously issued guidance addressing deferment and skip-a-pay programs for consumer loans and guidance encouraging credit unions to work with their members to help alleviate the economic uncertainty surrounding the COVID-19 National Emergency. This Guidance addresses loan loss-mitigation for real estate backed loans; however, this may also be applicable to non-real estate backed loans.

The Iowa Consumer Credit Code is silent regarding loss-mitigation for real estate secured loans.[1] Likewise, Regulation Z is not applicable, unless the loss-mitigation constitutes a full refinance. Each loan is a contract with corresponding contract law considerations. Therefore, the primary considerations regarding loss-mitigation of real estate secured loans are contractual obligations between the credit union and the borrower and regulatory considerations regarding Regulation X and Troubled Debt Restructuring, systemic risk considerations as well as safety and soundness.

Regulator Expectations:

1. Negative Amortization: Credit unions should attempt to avoid negative amortization whenever possible. If not possible due to the borrower's financial situation, credit unions must fully and completely explain negative amortization to the borrower and document this.
2. Regulation X: The Division will review Regulation X compliance in a manner consistent with the Interagency Statement issued on April 3,2020. See below for further details.
3. Documentation: The Division expects credit unions to fully document any approved loss-mitigation plan either through completed applications, agreement, or program parameters. Any denial of a loss-mitigation request must be equally documented and credit unions should consider whether a denial requires an adverse action form.

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[1] The Iowa Consumer Code only applies to HELOCs and second mortgages under the jurisdictional limit. Changing terms on HELOCs could implicate the Iowa Consumer Credit Code, but not if they are beneficial to the borrower or agreed to by the borrower.

4. Communication to the borrower: Credit unions must fully communicate to borrowers how their individual loss-mitigation will work; when their payment will resume; what the payment will be in the future; whether they will be disqualified from future loss-mitigation and for how long (and continue to communicate if this determination changes in the borrowers favor based on the length of the National Emergency); what will happen regarding escrow accounts, interest, and taxes; etc. Failure to fully and clearly communicate the changes to the borrower's loan may cause regulatory and legal problems for the credit union in the future.
5. Liquidity concerns: The Division expects all credit unions to be monitoring their liquidity and have an established plan to address liquidity needs.
6. Loss-mitigation length: The Division's guidance regarding loss-mitigation is limited to short-term arrangements, meaning 6 months or less; however, this does not prohibit longer loss-mitigation. Therefore, any loans requiring payments other than monthly must be specifically considered by the credit union to determine whether a loss-mitigation exceeds the 6-month timeframe. As an example, deferment of payment on a loan with one required annual payment will not receive the same deferential review from the Division as a deferment on a loan requiring monthly payments.
7. Credit risk: Credit unions should maintain appropriate allowance for loan and lease losses or credit losses as required. Credit unions should evaluate each approved loss-mitigation and consider whether a corresponding increase in their allowance account is necessary.
8. Consumer Protection: When considering loss-mitigation options, credit unions must comply with consumer protection requirements including the fair lending and equal credit laws. The Division will review programs for evidence of discrimination and proper communication with borrowers, but will not otherwise take issue with consumer compliance provided that the circumstances were related to the National Emergency and that credit unions made good faith efforts to support borrowers and comply with consumer protection requirements.
9. Reputation risk: Credit unions have no authority to deny a forbearance request for federally backed mortgages under the CARES Act. This places the credit union in a difficult scenario as members may know about the protections for federally backed mortgages and expect the same deferential treatment. While a credit union is not required to modify a non-federally backed mortgage, credit unions are encouraged to work with their members. The Division will take a reasonable and respectful approach to evaluating each credit union's loss-mitigation decisions following the COVID-19 National Emergency provided no safety and soundness concerns are present.
10. Contract Considerations: A loss-mitigation is a contract regulated by contract law. As such, credit unions must strongly consider whether their documentation is adequate for their purposes and protects the credit union from potential litigation later.
    a. Loss-mitigation agreements must be in writing and must include evidence of the borrower's agreement or acceptance of the terms and conditions. The written agreement must reference the related mortgage note.
    b. Requirements for signature and attestation vary. Credit unions should consider whether their e-signature policies and procedures are adequate and consistent with State and Federal law before accepting electronic signatures.

11. Maturity limits, liens, recording: Credit unions are encouraged to consider how their loss-mitigation programs comply with loan maturity limits, the lifespan of the lien on the underlying property, and whether they will record any loss-mitigation agreement.
12. Insurance concerns: Real estate secured loans require special considerations for property insurance and flood insurance. Credit unions must understand how loss-mitigation actions implicate these insurance requirements.
13. Escrow considerations: Credit unions should continue to collect escrow and tax payments as part of the loss-mitigation work out if possible. If not able to collect escrow payments, the credit union must develop a plan for how escrow payments will be addressed.

4013 Exemptions: Pursuant to the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), federally insured Credit Unions have the option to continue following the Troubled Debt Restructuring rules or may suspend these requirements under U.S. Generally Accepted Accounting Principles (GAAP) for loss-mitigation related to the COVID-19 pandemic (hereinafter referred to as 4013 exemption). It is for the credit union to determine whether it will continue to comply with TDR and the Iowa Division of Credit Unions will not question that determination. See CARES Act Section 4013. Only certain loss-mitigations are eligible for the 4013 exemptions. In order for a loss-mitigation to meet the 4013 exemption, the loss-mitigation must be related to COVID-19, the loan must not have been more than 30 days past due as of December 31, 2019, the loss-mitigation must be executed between March 1, 2020 and the close of the applicable period under the CARES Act [the earlier of December 31, 2020 or 60 days after the termination of the National Emergency]. For loss-mitigation under the 4013 exemption, a credit union is not required to comply with the standards for Troubled Debt Restructuring for the extent of the loss-mitigation. The Division will not require a credit union to categorize all COVID-19 related loan loss-mitigation as TDR's if the 4013 exemption is applicable.

TDR: If the 4013 exemption is not applicable or the credit union elects not to follow the 4013 exemption, then the credit union must determine whether the loss-mitigation constitutes Troubled Debt Restructuring. A loss-mitigation or restructuring of the debt is classified as a TDR if the creditor approves a concession it would not otherwise consider due to economic or legal reasons related to financial difficulties of the borrower. See Financial Accounting Standards Board, Accounting Standards Codification Subtopic 310-10, Receivables – Troubled Debt Restructurings by Creditors. Pursuant to FFIEC and FASB guidance, short-term loss-mitigations made in response to COVID-19, made to borrowers who were current prior to any relief, and made in good faith are not TDRs. In accordance with Interagency guidance,[2] a credit union:

> may presume that borrowers are not experiencing financial difficulties at the time of the modification for purposes of determining TDR status, and thus no further TDR analysis is required for each loan modification in the program, if:
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> - The modification is in response to the National Emergency;
> - The borrower was current on payments at the time the modification

[2] https://www.ncua.gov/files/press-releases-news/interagency-statement-tdr-policy-revised.pdf

program is implemented;[3] and

- The modification is short-term (e.g., six months).[4]

Government mandated deferral programs and mortgage foreclosures related to COVID-19 are not subject toTDR.

Credit reporting: The CARES Act requires credit unions to report loan loss-mitigations resulting from the COVID-19 as "current" or in the same manner as reported before the loss-mitigation, unless the borrower brings the loan current. This requirement applies throughout the period of the loss-mitigation if the borrower complies the requirements of the loss-mitigation plan. This protection is available beginning January 31, 2020, and ends 120 days after enactment of the CARES Act, or 120 days after the date the national emergency declaration for the coronavirus is terminated, whichever occurs later.[5]

Regulation X: Regulation X does not require servicers to offer borrowers specific loss mitigation options or loan modifications and does not mandate any particular eligibility criteria. Rather, Regulation X sets forth notice provisions for borrowers who apply for loss-mitigation. Regulation X allows servicers to offer short-term loss-mitigation options based on complete or incomplete applications and servicers may offer loss mitigation options to a borrower who has not submitted an application at all, or to a borrower when the offer is not based on an evaluation of information submitted by the borrower in connection with a loss-mitigation application. See Statement on Supervisory Practices Regarding Financial Institutions and Consumers Affected by a Major Disaster or Emergency. Consistent with Regulation X a servicer may not need to send an incomplete application notice under 12 CFR 1024.41(c)(2) if the services offers a loss mitigation without requiring an application or considering any information provided by a borrower in connection with a loss mitigation application, because the offer of the loss mitigation was not based on an evaluation of an application. For more information review CFPB official commentary found here: https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1024/Interp-41/#41-c-2-Interp

However, if an application is required or evaluated Regulation X requires mortgage servicers to provide an acknowledgement of submitted application within 5 days of receipt of the application. Pursuant to Regulation X if an incomplete application for loss-mitigation is submitted (including for federal forbearance) the servicer must provide an acknowledgement notice within five days of receipt of the incomplete application, even if the borrower was offered a short-term mitigation option. Consistent with NCUA, the Iowa Division of Credit Unions will not take regulatory action against a credit union for failing to send such a notice within the 5 day required period, if the servicer offers a short-term mitigation option and the servicer sends the acknowledgement notice before the end of the mitigation period. See Joint Statement on Supervisory and Enforcement Practices Regarding the Mortgage Servicing Rules in Response to the COVID-19 Emergency and the CARES Act, published April 3, 2020.

[3] To be considered current the borrower must have been less than 30 days past due at the time of loss-mitigation.
[4] Short-term loss-mitigations are those lasting 6 months or less.
[5] This is not applicable to credit obligations which have been charged-off. CARES Act Section 4021.

https://www.ncua.gov/files/press-releases-news/interagency-statement-mortgage-servicing-policy-statement.pdf

With respect to other loss mitigation and early intervention and annual escrow statement requirements set forth in Regulation X, the Iowa Division of Credit Unions agrees not to take regulatory action against a credit union to the same extent NCUA has set forth in the Joint Statement on Supervisory and Enforcement Practices Regarding the Mortgage Servicing Rules in Response to the COVID-19 Emergency and the CARES Act, published April 3, 2020.
https://www.ncua.gov/files/press-releases-news/interagency-statement-mortgage-servicing-policy-statement.pdf

Loss-Mitigation Types:

1. Federally Backed Mortgages:

   a. Borrowers with "Federally backed mortgage loans" are eligible for forbearance programs, regardless of whether loans are delinquent pursuant to the CARES Act. As such, Borrowers experiencing a financial hardship due, directly or indirectly, to the COVID-19 National Emergency, may request a forbearance by submitting a request to their mortgage servicer and affirming that they are experiencing a financial hardship. Pursuant to the CARES Act, servicers must provide a forbearance allowing borrowers to defer their mortgage payments for up to 180 days, (borrowers may extend the forbearance an additional 180 days upon request, but may also request to shorten the forbearance) Servicers **must** provide a CARES Act forbearance if the borrower makes this request and affirms that the borrower is experiencing a financial hardship. Servicers **may not** require any additional information from the borrower before granting a forbearance under the CARES Act.

   During the forbearance no fees, penalties, or interest may be applied beyond the amounts scheduled or calculated under the original terms of the mortgage loan and as if the borrower made all payments on time and in full.

   b. Federally backed mortgages include "any loan which is secured by a first or subordinate lien on residential real property (including individual units of condominiums and cooperatives) designed principally for the occupancy of from one-to-four families that is insured by the Federal Housing Administration under title II of the National Housing Act (12 U.S.C. 1707 et seq.); insured under section 255 of the National Housing Act (12 U.S.C. 1715z–20); guaranteed under section 184 or 184A of the Housing and Community Development Act of 1992 (12 U.S.C. 1715z–13a, 1715z–13b); guaranteed or insured by the Department of Veterans Affairs; guaranteed or insured by the Department of Agriculture; made by the Department of Agriculture; or purchased or securitized by the Federal Home Loan Mortgage Corporation or the Federal National Mortgage Association. CARES Act, Pub. L. 116-136, section 4022(a)(2)." See CARES Act Section 4022.

c. Different rules apply for federally backed residential mortgages for multi-family properties with 5 units or more. Multi-family borrowers are eligible for forbearance for up to 30 days and may extend the forbearance for up to 2 additional 30 day periods, so long as the extension request is made during the covered period and at least 15 days prior to the end of the forbearance period.

d. For more information, review:

https://www.fanniemae.com/portal/covid-19.html

https://sf.freddiemac.com/about/covid19

https://mf.freddiemac.com/COVID-19/

2. Non-Federally Backed: Credit unions have significant discretion to implement prudent loss-mitigation programs consistent with this guidance and as long as the safety and soundness of the credit union is not implicated negatively. Credit unions must do their own due diligence with respect to loss-mitigation options they intend to offer members. This guidance does not constitute a comprehensive list and does not address regulatory compliance requirements. The following are some available loss-mitigation options:

a. Forbearance/Deferment/Extension: This agreement between a borrower and their lender creates a temporary-alternative payment schedule to reduce or suspend regular payments for a specific period of time. Credit unions must consider and communicate exactly what is suspended. There are several different aspects of a mortgage payment including 1. Principal, 2. Interest, 3. Escrow, 4. Taxes, 5. Applicable fees. Credit unions must communicate to the borrower how each of these payment components will be treated under a forbearance/deferment/extension.

b. Modifications: This agreement between the borrower and their lender which changes the original terms of the mortgage—such as payment amount, length of loan, interest rate, etc.

c. Additional loans: Credit Unions may consider granting additional loans to members to allow them to continue to make their mortgage payments. Credit unions must specifically consider whether they will disburse the loan funds to the member directly or hold the funds to ensure payment under the mortgage. Also consider the terms, whether secured or unsecured, and that the additional loan does not constitute predatory lending.

d. Repayment plan: Repayment plans are agreements in which any past-due amount will be spread out over a set time frame (e.g., 3, 6, 9 months) and added on to the existing mortgage payments. Agreements outline how a borrower is going to repay the past-due amount, such as the length of the repayment period and the specific terms. In order to qualify as short-term the repayment plan is limited to repayment of no more than three months of past due payments over a period lasting no more than six months. See Regulation X, Comment 41(c)(2)(iii)-4.

e. Fee waiver: Credit unions have broad discretion to waive fees for their members.

3. HELOC: For additional information see https://www.ncua.gov/files/letters-credit-unions/HELOC-Interagency-Guidance-20140702.pdf

a. Modification: See 12 CFR § 1026.40. No creditor may change the annual percentage rate on a HELOC unless the change is based on an index outside the creditor's control and the index is available to the public, this prohibition includes agreements between the borrower and creditor. As a general rule, a creditor may not change the terms of a plan after it is opened, however, a creditor may change the terms if the borrower expressly agrees in writing to the change at the time the change is made. See 12 CFR § 1026.40(f)(3). Whenever a term required to be disclosed under § 1026.6(a) is changed or the required minimum periodic payment is increased, the creditor must mail or deliver notice of the change to each consumer who may be affected at least 15 days prior to the effective date of the change. The 15-day requirement is not applicable if the borrower agreed to the change; however, notice is still required before the effective date of the change. 12 CFR § 1026.9(c). Notice requirements are not applicable for changes reducing any component of a finance or other charge. 12 CFR § 1026.9(c). However, if the modification extends the term of the loan and the loan is outside the draw period, flood insurance provisions may be applicable.

b. Restrictions on the line of credit: A creditor may prohibit additional extensions of credit or reduce the line of credit if any of the following are found:

(A) The value of the dwelling that secures the plan declines significantly below the dwelling's appraised value for purposes of the plan;
(B) The creditor reasonably believes that the consumer will be unable to fulfill the repayment obligations under the plan because of a material change in the consumer's financial circumstances;
(C) The consumer is in default of any material obligation under the agreement;
(D) The creditor is precluded by government action from imposing the annual percentage rate provided for in the agreement;
(E) The priority of the creditor's security interest is adversely affected by government action to the extent that the value of the security interest is less than 120 percent of the credit line; or
(F) The creditor is notified by its regulatory agency that continued advances constitute an unsafe and unsound practice.

See 12 CFR § 1026.40(f)(3)(vi). Credit unions must perform their own due diligence and review the commentary regarding how these provisions are satisfied. Credit unions are required to provide notice to the borrower no more than three business days after the action is taken and must include specific reasons for the action. If the creditor requires the borrower to request reinstatement of credit privileges, this must be included in the notice. 12 CFR § 1026.9(c)(1)(iii).

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