Case Studies and Policy Changes

FHFA Relaxes Standards for GSE Mortgage Servicers

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On April 21, the Federal Housing Finance Agency (FHFA) announced that it was changing standards for mortgage servicers in an effort to reduce burdens brought on by drastic increases in mortgage nonpayment. Quickly following, on April 22, the FHFA announced that Fannie Mae and Freddie Mac would purchase some mortgages in forbearance due to COVID-19.

New forbearance policies under the CARES Act are creating liquidity issues for mortgage servicers. Typically, mortgage servicers collect payments of mortgage principal and interest from borrowers whose mortgages are in mortgage-backed security (MBS) pools and use the funds to make payments to investors who contractually own the rights to the cash flows from the mortgages in the pool. Fannie Mae usually requires that the servicer advance payments of loan principal and interest for up to 12 months, even if a borrower is in arrears. Freddie Mac only requires that servicers advance interest-only payments for up to four months.

The new changes reduce the required advance period under Fannie Mae mortgages from 12 months to four months. This aligns the advance periods for all Fannie Mae and Freddie Mac single-family mortgages. The new policies apply to all single-family mortgages backed by Fannie Mae or Freddie Mac and to all servicers, regardless of type or size.

While Fannie and Freddie usually buy loans more than four months in arrears out of MBS pools to replace them with performing loans, the FHFA has instructed the GSEs to treat loans in COVID-19 forbearance as if they were subject to temporary natural disaster relief, which would allow the loans to remain in the MBS pool for the period of forbearance. The change in treatment reduces liquidity demands on the two government-sponsored enterprises (GSEs).

Also, as of April 22, FHFA announced that Fannie and Freddie would purchase mortgages that have gone into forbearance almost immediately after closing. FHFA had previously treated such loans as ineligible for purchase. Mortgages originated between February 1, 2020, and May 31, 2020, are eligible for purchase. Mortgages cannot be more than 30 days delinquent. The GSEs will price these purchases to account for the increased risk of the mortgage in forbearance. By relaxing mortgage purchasing standards, FHFA hopes to encourage mortgage origination in a slow credit market, in which servicers are unwilling to originate mortgages for fear that GSEs may not buy them.

Through the CARES Act, the government made forbearance available to all borrowers with federally backed single-family or multi-family mortgages. The forbearance period for single-family mortgages can extend as long as a year. As of April 19, the share of loans in forbearance rose to 6.99%, up from 0.25% on March 6. Industry officials expect forbearance requests will continue to rise with unemployment. As COVID-19 continues to depress demand and employment, it remains unclear when homeowners in forbearance may be able to resume mortgage payments. The Mortgage Bankers Association estimates that in a worst-case scenario, servicers might need to fund as much as $75-100 billion in advances.

Though these changes in regulation provide a welcomed and needed reprieve for mortgage servicers, servicers continue to push for a mortgage liquidity facility to ease strain on cash flows during the forbearance period. Beginning in late March, many called for the Federal Reserve to set up a mortgage liquidity facility to ease the liquidity pressures on mortgage servicers that emerged as a result of the CARES Act. On April 8, a bipartisan group of senators explicitly requested that the Federal Reserve set up a mortgage liquidity facility, something the central bank has resisted doing. Mortgage experts believe that the Federal Reserve will create a funding facility, but not until there is a meaningful increase in forbearance activity.