110TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { 110–615

EMERGENCY MORTGAGE LOAN MODIFICATION ACT OF 2008

MAY 1, 2008.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. FRANK of Massachusetts, from the Committee on Financial Services, submitted the following

REPORT

[To accompany H.R. 5579]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 5579) to remove an impediment to troubled debt restructuring on the part of holders of residential mortgage loans, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

CONTENTS

	Page
Amendment	2
Purpose and Summary	3
Summary of Major Provisions	3
Background and Need for Legislation	4
Hearings	5
Committee Consideration	6
Committee Votes	6
Committee Oversight Findings	6
Performance Goals and Objectives	6
New Budget Authority, Entitlement Authority, and Tax Expenditures	7
Committee Cost Estimate	7
Congressional Budget Office Estimate	7
Federal Mandates Statement	8
Advisory Committee Statement	8
Constitutional Authority Statement	8
Applicability to Legislative Branch	8
Earmark Identification	8
Section-by-Section Analysis of the Legislation	8

69–006

AMENDMENT

The amendment is as follows:
Strike all after the enacting clause and insert the following:

SECTION 1. SHORT TITLE.

This Act may be cited as the “Emergency Mortgage Loan Modification Act of 2008”.

SEC. 2. SAFE HARBOR FOR QUALIFIED LOAN MODIFICATIONS OR WORKOUT PLANS FOR CERTAIN RESIDENTIAL MORTGAGE LOANS.

(a) STANDARD FOR LOAN MODIFICATIONS OR WORKOUT PLANS.—Absent contractual provisions to the contrary—

(1) the duty to maximize, or to not adversely affect, the recovery of total proceeds from pooled residential mortgage loans is owed by a servicer of such pooled loans to the securitization vehicle for the benefit of all investors and holders of beneficial interests in the pooled loans, in the aggregate, and not to any individual party or group of parties; and

(2) a servicer of pooled residential mortgage loans shall be deemed to be acting on behalf of the securitization vehicle in the best interest of all investors and holders of beneficial interests in the pooled loans, in the aggregate, if for a loan that is in payment default under the loan agreement or for which payment default is imminent or reasonably foreseeable, the loan servicer makes reasonable and documented efforts to implement a modification or workout plan or, if such efforts are unsuccessful or such plan would be infeasible, engages in other loss mitigation, including accepting a short payment or partial discharge of principal, or agreeing to a short sale of the property, to the extent that the servicer reasonably believes the particular modification or workout plan or other mitigation actions will maximize the net present value to be realized on the loan, including over that which would be realized through foreclosure.

(b) SAFE HARBOR.—Absent contractual provisions to the contrary, a servicer of a residential mortgage loan that acts in a manner consistent with the duty set forth in subsection (a), shall not be liable for entering into a qualified loan modification or workout plan, to—

(1) any person, based on that person’s ownership of a residential mortgage loan or any interest in a pool of residential mortgage loans or in securities that distribute payments out of the principal, interest and other payments in loans on the pool;

(2) any person who is obligated pursuant to a derivatives instrument to make payments determined in reference to any loan or any interest referred to in paragraph (1); or

(3) any person that insures any loan or any interest referred to in paragraph (1) under any law or regulation of the United States or any law or regulation of any State or political subdivision of any State.

(c) RULE OF CONSTRUCTION.—No provision of this section shall be construed as limiting the ability of a servicer to enter into loan modifications or workout plans other than qualified loan modification or workout plans.

(d) DEFINITIONS.—For purposes of this section, the following definitions shall apply:

(1) QUALIFIED LOAN MODIFICATION OR WORKOUT PLAN.—The term “qualified loan modification or workout plan” means a modification or plan that—

(A) is scheduled to remain in place until the borrower sells or refinances the property, or for at least 5 years from the date of adoption of the plan, whichever is sooner;

(B) does not provide for a repayment schedule that results in negative amortization at any time; and

(C) does not require the borrower to pay additional points and fees.

(2) NEGATIVE AMORTIZATION.—For purposes of paragraph (1), the term “negative amortization” does not include the capitalization of delinquent interest and arrearages.

(3) RESIDENTIAL MORTGAGE LOAN DEFINED.—The term “residential mortgage loan” means a loan that is secured by a lien on an owner-occupied residential dwelling.

(4) SECURITIZATION VEHICLE.—The term “securitization vehicle” means a trust, corporation, partnership, limited liability entity, special purpose entity, or other structure that—

(A) is the issuer, or is created by the issuer, of mortgage pass-through certificates, participation certificates, mortgage-backed securities, or other

similar securities backed by a pool of assets that includes residential mortgage loans; and

(B) holds such loans.

(e) EFFECTIVE PERIOD.—This section shall apply only with respect to qualified loan modification or workout plans initiated prior to January 1, 2011.

PURPOSE AND SUMMARY

H.R. 5579, the Emergency Mortgage Loan Modification Act of 2008, was introduced on March 11, 2008, by Mr. Castle and Mr. Kanjorski. The purpose of the bill is to clarify certain existing duties and responsibilities of mortgage loan servicers in effecting modifications of mortgage loans that are in default or for which default is imminent. The bill also provides a safe harbor from lawsuits by investors for mortgage servicers who engage in specified loan modifications and workouts, consistent with those duties.

SUMMARY OF MAJOR PROVISIONS

Servicer duty of care

The duties and responsibilities of servicers of securitized mortgage loan pools are established in contracts called servicing agreements or pooling and servicing agreements (Pooling and Servicing Agreements). Such agreements generally include a requirement that a servicer follow accepted servicing practices and procedures. While there is a degree of standardization among Pooling and Servicing Agreements regarding some provisions, other provisions may vary substantially. For instance, some agreements will give servicers broad authority to engage in loss mitigation on loans that are in default or for which default is reasonably foreseeable, so long as the servicers' actions are in the best interests of the security holders. Other agreements may spell out the types of permissible modifications or limit the number or timing of modifications of loans in the pool.

Inadequate resources to identify, evaluate, conduct outreach for and process the volume of loans in or near default have plagued servicer efforts to engage in timely and meaningful loan modifications in the face of the current foreclosure crisis. Servicers say they are further hindered by uncertainty about what modification actions may be permitted under their agreements, and by the fear of litigation by investors.

The servicer duty provisions are intended to provide a measure of clarity and certainty to servicers by codifying concepts that are consistent with existing contractual obligations. The legislation makes clear that, absent any contractual provisions to the contrary, the duty of the servicer to maximize, or not adversely affect, the recovery of proceeds from pooled mortgage loans is owed for the benefit of investors in the aggregate, and not to any individual investor or group of investors. This articulation of the servicer duty is consistent with existing Pooling and Servicing Agreements, and with servicer best practices as developed by the American Securitization Forum (ASF) and reflected in their "Statement of Principles, Recommendations and Guidelines for the Modification of Securitized Subprime Residential Mortgage Loans" (June 2007). The Committee expects that this clarification will reduce servicer concerns about liability to investors in securitization tranches that may be disadvantaged by a servicer's loss mitigation actions.

The legislation also clarifies that, absent contrary contractual provisions, a servicer is acting in the best interest of all investors if it implements a modification or workout plan or engages in other loss mitigation efforts, including accepting a short payment or short sale, for a loan that is in default or for which default is imminent or reasonably foreseeable, to the extent the servicer reasonably believes the modification will maximize the net present value to be realized on the loan, including over that which would be realized through foreclosure. Again, this generally is consistent with existing Pooling and Servicing Agreements, as well as with the ASF principle that loan modifications are important loss mitigation tools and other loss mitigation alternatives, including short sales and short payoffs, are useful. The Committee expects that these changes will clear the way for servicers to initiate long-term sustainable loan modifications that will be a benefit to all parties.

Safe harbor

The legislation provides a safe harbor from lawsuits by investors for servicers that meet their prescribed duties, and enter into "qualified loan modification or workout plans." "Qualified loan modification or workout plan" is defined as a plan that: (1) remains in place for at least five years, unless the borrower sells the property or refinances the loan during that time; (2) includes repayment schedules that do not result in negative amortization; and (3) does not require the borrower to pay additional points and fees. These conditions are intended to result in long-term, sustainable and affordable mortgage obligations for homeowners and a continued stream of income for investors. The term "negative amortization" is not intended to include extensions of loan terms to repay delinquent interest and arrearages, so long as the structure does not at any time result in negative amortization; that is, the amounts are not added back into the loan principal and the outstanding balance of the loan does not increase. The Committee hopes, however, that servicers will carefully consider forgiveness of arrearages in appropriate circumstances.

The safe harbor would apply only to owner-occupied residential mortgage loans, and only to qualified modifications or workout plans initiated prior to January 1, 2011.

The legislation does not create statutory preferences for loss mitigation activities, nor is it intended to limit the ability of servicers to enter into modifications or workouts other than those referenced in the legislation.

The legislation would provide a safe harbor only from investor lawsuits and only for loan modification or workout plans having the specified characteristics. It is the Committee's intent that the legislation would not affect the ability of consumers or borrowers to pursue claims against lenders or servicers for fraud or for discriminatory or abusive lending practices.

BACKGROUND AND NEED FOR LEGISLATION

The number of American families facing or at risk of foreclosure has grown dramatically during the current upheaval in the mortgage and housing markets. According to the Mortgage Bankers Association (MBA), 5.82 percent of all loans on single-family properties outstanding in the fourth quarter of 2007 were delinquent,

the highest total delinquency rate in the MBA survey in over 20 years. The percentage of loans in the foreclosure process also stands at record highs. A complex mix of circumstances has made it difficult for borrowers to restructure or refinance their loans, including that many of those loans were securitized into asset-backed securities and sold in the secondary market.

One of the reasons given for the slow pace of loan modifications is that some servicers are concerned about legal liability to investors based on those modifications. While servicers have been trying to work with borrowers under a variety of programs, many of these efforts have been in the form of short-term extensions of the initial, starter or "teaser" rates, or temporary repayment plans that do not provide the long-term stability needed by borrowers, investors or the markets.

This legislation is designed to facilitate loan modifications and workouts by clarifying mortgage loan servicers' responsibilities in effecting modifications of mortgage loans that are in default or for which default is imminent, and providing a safe harbor from lawsuits by investors for mortgage servicers who engage in specified loan modifications and workouts.

HEARINGS

The Financial Services Committee held a hearing on December 6, 2007, titled "Accelerating Loan Modifications, Improving Foreclosure Prevention and Enhancing Enforcement" at which the Committee considered a previous version of the bill, H.R. 4178, introduced by Mr. Castle on November 14, 2007. The following witnesses testified: The Honorable Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation; The Honorable Randall S. Kroszner, Governor, Board of Governors of the Federal Reserve System; The Honorable John C. Dugan, Comptroller, Office of the Comptroller of the Currency; The Honorable Gigi Hyland, Board Member, National Credit Union Administration; Mr. Scott M. Polakoff, Senior Deputy Director and Chief Operating Officer, Office of Thrift Supervision; Mr. Mark E. Pearce, North Carolina Deputy Commissioner of Banks, on behalf of the Conference of State Bank Supervisors; Mr. Tom Deutsch, Deputy Executive Director, American Securitization Forum; Ms. Faith Schwartz, Executive Director, HOPE NOW Alliance; Mr. Hilary O. Shelton, Director, National Association for the Advancement of Colored People; Mr. Damon Silvers, Associate General Counsel, AFL–CIO; Dr. Richard Kent Green, Oliver T. Carr, Jr. Chair of Real Estate Finance, The GW School of Business, George Washington University; Mr. Laurence E. Platt, Partner, K&L Gates, on behalf of the Securities Industry and Financial Markets Association; Mr. Michael Calhoun, President, Center for Responsible Lending; and Mr. John Taylor, Vice President for Policy, National Community Reinvestment Coalition.

At a hearing of the Financial Services Committee on April 9, 2008, titled "Using FHA for Housing Stabilization and Homeownership Retention," provisions of H.R. 5579 were addressed by members and witnesses. Specifically, the Honorable Sheila Bair, Chairman, Federal Deposit Insurance Corporation, and the Honorable John C. Dugan, Comptroller, Office of the Comptroller of the Currency, expressed support for the legislation. Other witnesses at the

hearing included: The Honorable John M. Reich, Director, Office of Thrift Supervision; The Honorable Randall S. Kroszner, Governor, Board of Governors of the Federal Reserve System; The Honorable Brian Montgomery, Assistant Secretary for Housing-Federal Housing Commissioner, United States Department of Housing and Urban Development; Mr. Brian Wesbury, Chief Economist, First Trust Advisors L.P.; Dr. Alan S. Blinder, Ph.D., Gordon S. Rentschler Memorial Professor of Economics and Public Affairs, Princeton University; and Dr. Allen Sinai, Chief Global Economist, Strategist and President, Decision Economics, Inc.

The Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises held a legislative hearing on April 15, 2008, titled "H.R. 5579, The Emergency Mortgage Loan Modification Act of 2008." The following witnesses testified: Mr. Ralph DaLoisio, Managing Director, Natixis Structured Finance Group, on behalf of the American Securitization Forum; Mr. Robert E. Story, Jr., President, Seattle Financial Group, and Vice Chairman, Mortgage Bankers Association, on behalf of the Mortgage Bankers Association; and Mr. Marlo A. Young, Partner, Thacher Proffitt & Wood LLP.

COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on April 23, 2008, and ordered H.R. 5579, the "Emergency Mortgage Loan Modification Act of 2008", as amended, favorably reported by a voice vote.

COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. No record votes were taken in conjunction with the consideration of this legislation. A motion by Mr. Kanjorski to report the bill, as amended, to the House with a favorable recommendation was agreed to by a voice vote.

During the consideration of the bill, the following amendment was considered:

An amendment by Mr. Kanjorski, No. 1, a manager's amendment making various technical and substantive changes, was agreed to by a voice vote.

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee has held hearings and made findings that are reflected in this report.

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee establishes the following performance related goals and objectives for this legislation:

To the extent that existing duties and responsibilities of mortgage loan servicers are clarified, and a safe harbor from lawsuits by investors for mortgage servicers who engage in specified loan

modifications and workouts is created, mortgage servicers will increase efforts to initiate long-term sustainable loan modifications.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee adopts as its own the estimate of new budget authority, entitlement authority, or tax expenditures or revenues contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

COMMITTEE COST ESTIMATE

The Committee adopts as its own the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATE

Pursuant to clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974:

APRIL 28, 2008.

Hon. BARNEY FRANK,
Chairman, Committee on Financial Services,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 5579, the Emergency Mortgage Loan Modification Act of 2008.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susanne S. Mehlman.

Sincerely,

PETER R. ORSZAG.

Enclosure.

H.R. 5579—Emergency Mortgage Loan Modification Act of 2008

H.R. 5579 would protect mortgage servicers from legal liability if they perform loan modifications according to specific criteria established under the legislation. CBO estimates that enacting this legislation would have no significant impact on the federal budget and would not affect direct spending or revenues.

Residential mortgages are often pooled together and sold to investors as securities. The pools of loans are overseen by mortgage servicers, who have a fiduciary responsibility to maximize returns to the investors. Many pooling and servicing agreements give servicers authority to modify the terms of securitized loans if that action is in the interest of maximizing the value of the loan pool, but some agreements are more restrictive. Pooling and servicing agreements can be amended with the consent of investors. However, not all investors in mortgage-backed securities share losses equally, which may limit servicers' ability to obtain permission to modify the terms of loans to ensure maximum value for all inves-

tors. H.R. 5579 would provide legal protection for servicers of mortgage pools when they modify mortgages.

H.R. 5579 contains both intergovernmental and private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA), but CBO estimates that the costs of those mandates would not exceed the annual thresholds for intergovernmental or private-sector mandates established in UMRA ($68 million and $136 million, respectively, in 2008, adjusted annually for inflation). By preventing investors, both public and private, from seeking damages on grounds that the servicing agreement had been violated, the legislation would impose a mandate on governmental and private-sector entities that invest in pooled residential mortgages. CBO concludes, however, that servicers would be unlikely to alter mortgages in ways that would be significant enough to cause investors to seek damages because they would still be required to ensure the greatest return to investors under their fiduciary obligations.

The CBO staff contact for this estimate is Susanne S. Mehlman. This estimate was approved by Theresa Gullo, Deputy Assistant Director for Budget Analysis.

FEDERAL MANDATES STATEMENT

The Committee adopts as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act.

ADVISORY COMMITTEE STATEMENT

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act were created by this legislation.

CONSTITUTIONAL AUTHORITY STATEMENT

Pursuant to clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee finds that the Constitutional Authority of Congress to enact this legislation is provided by Article 1, section 8, clause 1 (relating to the general welfare of the United States) and clause 3 (relating to the power to regulate interstate commerce).

APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of section 102(b)(3) of the Congressional Accountability Act.

EARMARK IDENTIFICATION

H.R. 5579 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9 of rule XXI.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

Section 1. Short title

This section establishes the short title of the bill, the "Emergency Mortgage Loan Modification Act of 2008."

Section 2. Safe harbor for qualified loan modification or workout plans for certain residential mortgage loans

Subsection (a)—Standard for loan modifications or workout plans

This subsection sets forth the duty of loan servicers to maximize or not adversely affect recovery of proceeds from pooled residential mortgage loans on behalf of the securitization vehicle and in the best interest of the investors in the aggregate, without regard to the interests of individual investors or tranches. The duty applies only in the absence of contrary contractual provisions.

This subsection further provides that a servicer acts in the best interest of all investors if, for loans in default or for which default is imminent or reasonably foreseeable, it makes reasonable efforts to implement a loan modification or workout plan, or engages in other loss mitigation efforts, including acceptance of short payments, agreeing to short sales, or accepting partial discharges of principal. The servicer must reasonably believe that its loss mitigation actions will maximize the net present value of the loan, including over the value that would be realized through foreclosure.

Subsection (b)—Safe harbor

This subsection provides that a servicer that acts in a manner consistent with the duty in the legislation will not be liable to investors or insurers for entering into qualified loan modification or workout plans. The safe harbor would apply only in the absence of contrary contractual provisions. Investors subject to the provision are those who own residential mortgage loans, hold any interest in a pool of residential mortgage loans or in pass-through securities, or through derivatives instruments the payments of which are determined in reference to residential mortgage loans, pools or other securities.

Subsection (c)—Rule of construction

This subsection specifies that nothing in the legislation limits the ability of loan servicers to enter into other types of modifications or workouts.

Subsection (d)—Definitions

This subsection defines terms used in the legislation, including "securitization vehicle," "residential mortgage loan," and "qualified loan modification or workout plan." "Residential mortgage loan" is defined as a loan secured by an owner-occupied residential dwelling. This subsection also defines "qualified loan modification or workout plan" as a plan that (1) is scheduled to remain in place for at least five years, unless the borrower sells the property or refinances the loan; (2) does not include repayment schedules that result in negative amortization; and (3) does not require the borrower to pay additional points and fees. For purposes of this subsection, negative amortization does not include capitalization of delinquent interest or arrearages.

Subsection (e)—Effective date

Applies only to qualified loan modification or workout plans initiated prior to January 1, 2011.