

Protecting Homeownership From the Impact of COVID-19

May 10, 2021

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We would like to thank the National Association of REALTORS® for providing financial support for this paper. The opinions expressed are our own, and do not necessarily reflect the positions of NAR.



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About the National Community Stabilization Trust

The National Community Stabilization Trust ("NCST") strengthens communities by focusing on the health of the residential housing market. It does so by providing community-based buyers an exclusive first look opportunity to acquire and rehab distressed properties, by developing sources of capital for those buyers, and by advocating for policies that prevent neighborhood blight, promote stable communities, and support affordable homeownership.

About the National Fair Housing Alliance

Founded in 1988 and headquartered in Washington, DC, the National Fair Housing Alliance ("NFHA") is the only national organization dedicated solely to ending discrimination in housing. NFHA is the voice of fair housing and works to eliminate housing discrimination and to ensure equal housing opportunity for all people through leadership, education and outreach, membership services, public policy initiatives, community development initiatives, advocacy, tech equity, and enforcement.



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EXECUTIVE SUMMARY

As the United States confronts the COVID-19 pandemic, we must chart a different course to protect homeownership than we did during our response to the Great Recession.

During the Great Recession and its aftermath, almost eight million homeowners throughout the country lost their homes to foreclosure.¹ It is estimated that households lost as much as \$20 trillion in equity.² Vacant and abandoned homes blighted many neighborhoods throughout the country, bringing down home values, dampening previously healthy housing markets, and costing municipalities dearly in lost tax revenue and increased expenditures on public safety. More than five million homes that were originally owner-occupied transitioned to investor-owned rental homes between 2006 and 2017, reducing the number of home sales by about 270,000 each year, or about five percent of typical annual sales during this period.³

Nearly all of this economic pain has disproportionately affected communities of color.⁴ People of color were more likely to experience foreclosure and wealth loss, and the Black homeownership rate has still not returned to pre-crisis levels. Once foreclosed homes entered REO (real estate owned, aka bank-owned) portfolios, some lenders maintained and marketed properties in a discriminatory manner in communities of color while maintaining them properly in White communities. Out-of-town investors purchased many REO homes (or non-performing mortgages) and rented them out in these neighborhoods without making needed repairs. As a result, the racial wealth and homeownership gaps widened.

Today, we face another housing crisis. This one is not caused by unsafe mortgages and excess leverage in the capital markets. Rather, the COVID-19 pandemic is wreaking havoc on employment and quite literally killing hundreds of thousands of Americans. Yet, like the Great Recession, this crisis has a high potential to damage families and neighborhoods and endanger homeownership opportunities both now and after the pandemic. Predictably, this crisis too is impacting households and communities of color the hardest. This is why it is critical that policymakers, federal agencies, and financial services providers evaluate the programs and policies they implement during and after the pandemic through an equity lens to ensure that consumers of color will not be under served.

Managing this crisis to achieve racially equitable outcomes for households and neighborhoods will require us to be proactive. Fortunately, the industry has learned a lot from the financial crisis, which

¹ "United States Residential Foreclosure Crisis: Ten Years Later," CoreLogic, March 2017,

<https://www.corelogic.com/research/foreclosure-report/national-foreclosure-report-10-year.pdf>.

² "The Financial Crisis Response in Charts," U.S. Department of the Treasury, April 2012, https://www.treasury.gov/resource-center/data-chart-center/Documents/20120413_FinancialCrisisResponse.pdf.

³ Aaron Terrazas, "Rising Single-Family Rentals Dampening Home Sales," Zillow, December 12, 2017, <https://www.zillow.com/research/single-family-rentals-bottom-17595/>.

⁴ We recognize that there is not universal agreement on the appropriate race or ethnicity labels for the diverse populations in the United States, or even on whether or not particular labels should be capitalized. We intend in all cases to be inclusive, rather than exclusive, and in no case intend to diminish the significance of the viewpoint of any person or to injure a person or group through our terminology. For purposes of this report, we have utilized the following language except in cases where a resource, reference, case, or quotation may use alternate terminology: Black, Native American, Latino, Asian American, and White. In lieu of the term "minority neighborhood," we use the term "community of color."



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means that we have some good ideas on what policies will work. These policies fall broadly into two buckets: policies related to people and policies related to properties.

POLICIES RELATED TO PEOPLE

The pandemic has damaged the ability of households to pay their mortgages, putting their ability to sustain homeownership at risk. As a result, we see rising delinquencies across all channels, with particular concentration in Federal Housing Administration (“FHA”) borrowers and borrowers with Veterans’ Administration (“VA”)-backed loans. These borrowers are most at risk of having low or negative equity in their property, although far fewer homeowners now will find themselves underwater than during the Great Recession.

Notably, the initial policy response to this problem was swift and highly effective: the CARES Act forbearance program created by Congress in March 2020, which gave borrowers with federally-backed mortgages the ability to pause their mortgage payments for 12 (now 18) months. This option has provided a critical lifeline to many borrowers suffering from temporary hardships due to the pandemic. However, it leaves out borrowers with private mortgages and those at risk of tax foreclosure. As of January 2021, about 2.7 million households are on a mortgage forbearance, down from a peak of about 4.8 million in May 2020. Most borrowers who have exited forbearance so far have been able to resolve their hardship and begin making mortgage payments again, but the Mortgage Bankers Association reports that 13.9 percent of borrowers exit forbearance without a plan. In addition, the majority of borrowers who entered into forbearance remain in that status.

Whether the forbearance regime prevents most foreclosures and unnecessary home loss or whether it simply delays them will depend on the availability of affordable post-forbearance options and skilled work by mortgage servicers. That said, there is no doubt that some borrowers will lose their homes due to COVID-19 either through a forced sale or through foreclosure.

On the other hand, the pandemic and policies to respond to it have caused a contraction in mortgage credit availability, which prevents some households from becoming homeowners when low interest rates make homeownership more attainable.

To address these issues, we recommend the following strategies for preventing foreclosures and ensuring that households can access affordable and sustainable mortgage credit.

- **Increase access to COVID mortgage forbearances** through several policy changes, including extending forbearance protections to the entire mortgage market;
- **Give borrowers the post-forbearance options best suited for their circumstances**, including standardizing options across the market and giving borrowers the option of choosing how they resolve their COVID hardships;
- **Encourage communication between borrowers and mortgage servicers** by improving servicer capacity and government oversight of servicer execution;
- **Ensure the Homeowner Assistance Fund meets its goals** by avoiding restrictive program requirements, addressing program bottlenecks, and proactively working to provide funds to borrowers who could benefit from them; and,
- **Support alternatives to foreclosure for those who need them** by educating borrowers about their options and making those programs easy to access.



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We make the following recommendations to ensure that households can access affordable and sustainable mortgage credit:

- **Prevent the pandemic from negatively affecting consumer credit scores**, including having furnishers of data carefully monitor how they report foreclosure avoidance strategies;
- **Allow borrowers to access new mortgages after forbearance and foreclosure**; and,
- **Eliminate forbearance penalties that decrease access to credit.**

POLICIES RELATED TO PROPERTIES

Housing sales have boomed during the pandemic due to record low interest rates and many families moving to larger quarters or homes with office space. While that has been excellent news for existing homeowners, lenders, and other industry participants, demand for homes has far outstripped supply, leading to home prices that are higher than ever. As of the fourth quarter of 2020, median home prices increased by more than 10 percent over the past year in 88 percent of metro areas, and not a single metro area saw prices decline.⁵

For this reason, advocates for increasing homeownership, especially for families of color, cannot just focus on mortgage affordability. They must also concentrate on the serious supply shortage, which is especially acute in the lower value bands. Since the Great Recession, the U.S. has been underbuilding new housing, and by one estimate, we are 3.8 million homes short of where we need to be. One aspect of this problem is that since the financial crisis, homebuyers who require financing often lose out to cash buyers, many of whom are not owner-occupants. Some sellers, especially retirees, do not sell their home when they move but rent the property to receive a stream of income. Additionally, many homes are sold through processes that owner-occupants often do not use, such as foreclosure auctions and other sales on auction websites. As property sellers increasingly use auction sites to sell homes, the scales continue to tip in favor of the cash investor rather than a family with a mortgage.

Finally, for the few properties that do end up in REO portfolios, it is critical to pay attention to who is buying them and how those properties are maintained. In the aftermath of the Great Recession, we saw countless examples of foreclosed REO properties improperly maintained by the financial institutions that owned them, especially in communities of color. Poor maintenance practices damage neighborhoods and increase the likelihood that properties will be sold to investors to be used as rental properties rather than to owner-occupants.

To address these issues, we make the following recommendations:

- **Prioritize homeownership and neighborhood stabilization in distressed and REO sales** by implementing “First Look” programs that provide nonprofits and owner-occupants a time-limited exclusive opportunity to purchase and by making other reforms to note sales programs;
- **Properly maintain REO properties in all neighborhoods** by improving vendor oversight, using local vendors, and maintaining and marketing properties equally; and,

⁵ "All Metro Areas Saw Home Prices Rise during Fourth Quarter of 2020," National Association of REALTORS[®], February 11, 2021, <https://www.nar.realtor/newsroom/all-metro-areas-saw-home-prices-rise-during-fourth-quarter-of-2020>.



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- **Prevent zombie foreclosures and aggressively address vacancy problems** by discouraging investors from “walking away” from unprofitable properties and by using state and local tools.

As a country, we have the opportunity to learn from the mistakes made during the Great Recession. By preventing unnecessary foreclosures and home loss, maintaining access to credit, ensuring vacant properties do not blight communities, and leveling the playing field for owner-occupants to purchase homes, we can prevent the COVID-19 crisis from devastating homeownership and racial equity in housing markets.



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Chapter 1: The COVID-19 Crisis Matters for Homeownership

The United States is facing a significant public health and economic crisis caused by the COVID-19 pandemic and the resulting recession. Policymakers must take proactive steps to ensure that this crisis does not have the devastating effect on homeownership opportunities and racial equity in housing markets that the financial crisis did.

First, policies should prevent unnecessary foreclosures and the adverse impact they have on homeowners. Second, the pandemic should not result in an avoidable contraction of credit availability, preventing new households, especially households of color, from becoming homeowners. Third, when mortgage defaults or foreclosures do inevitably occur, properties should remain available for new families to access affordable homeownership.

A. Economic and Health Impacts of the COVID-19 Pandemic

Unlike the Great Recession—which was triggered by discriminatory, risky, and/or predatory lending practices, a massive home price boom and bust, lax regulation, and systemic weaknesses in the U.S. financial system—today's inability of many families to pay their mortgages is driven primarily by either income loss or additional expenses related to COVID-19.

At the outbreak of the pandemic, unemployment escalated dramatically to 14.7 percent in April 2020. While jobs began to return after the initial lockdown period, unemployment remains significantly elevated from pre-COVID levels. The Economic Policy Institute estimates that as of March 2021, 23.6 million workers, or nearly 15 percent of the workforce, were directly harmed by the coronavirus downturn because they were unemployed, had dropped out of the labor force, or had experienced a reduction in pay.⁶

New vaccine availability offers hope that the worst of the pandemic will be over before the end of 2021. However, even as the threat of serious illness recedes, it is likely to be months or even years before all borrowers experience a full economic recovery with incomes returning to pre-pandemic levels.

B. Non-White Households Are Disproportionately Harmed by the COVID-19 Pandemic

The pandemic has disproportionately harmed the health and economic security of households and neighborhoods of color.

Black, Indigenous, and Latino Americans are more likely to contract COVID-19, more likely to end up in the hospital, and more likely to die from the virus than their White counterparts.⁷ As of March 5, 2021, in the United States, the mortality rate for Blacks was one in every 555; for Indigenous Americans, one in every 390; for Latinos, one in every 680; for Pacific Islanders, one in every 565; for Asians, one in every

⁶ Elise Gould, "Strong job growth in March as vaccine distribution expands and the American Rescue Plan ramps up," Economic Policy Institute, April 2, 2021, <https://www.epi.org/blog/strong-job-growth-in-march-as-vaccine-distribution-expands-and-the-american-rescue-plan-ramps-up/>.

⁷ Samantha Artiga, Bradley Corallo, and Olivia Pham, "Racial Disparities in COVID-19: Key Findings from Available Data and Analysis," Kaiser Family Foundation, August 17, 2020, <https://www.kff.org/racial-equity-and-health-policy/issue-brief/racial-disparities-covid-19-key-findings-available-data-analysis>.



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1040; and for Whites, one in every 665.⁸ COVID-19 is the third-leading cause of death for Black Americans, and in 2020, more Black Americans died of COVID-19 than of diabetes, stroke, accidents, or pneumonia.

Some of these disparities are due to inequalities in health and access to medical care that existed long before the pandemic began. People of color were already more likely to have pre-existing conditions, less likely to have health insurance or paid sick leave, and less likely to have access to medical facilities. But resources specifically to address COVID-19 have also been distributed inequitably. People of color encounter more barriers to accessing testing for COVID-19,⁹ and they are also less likely to receive COVID-19 related healthcare or vaccinations.¹⁰

Another reason people of color are more affected by the virus is that they disproportionately work in front-line, essential jobs that put them at additional risk of contracting COVID-19. The Department of Labor found that, in 2017 and 2018, about 30 percent of White employees had jobs they could do from home, compared to 20 percent of Black workers and 16 percent of Latino workers. Sixty-one percent of workers in the top quarter of earners could work from home, while only nine percent of those in the bottom quarter could work from home.¹¹

Even as jobs have returned, the unemployment rate has consistently remained higher for Black and Latino households. As of March 2021, the Black unemployment rate remained above nine percent, and many more of these households lost wages or left the workforce.

Figure 1: Unemployment Rate by Race or Ethnicity	July 2020	Aug 2020	Sept 2020	Oct 2020	Nov 2020	Dec 2020	Jan 2021	Feb 2021	March 2021
White (any ethnicity)	9.2	7.3	7.0	6.0	5.9	6.0	5.7	5.6	5.4
Black or African-American (any ethnicity)	14.6	13.0	12.0	10.8	10.3	9.9	9.2	9.9	9.6

⁸ "Color of Coronavirus: COVID-19 Deaths Analyzed by Race and Ethnicity," APM Research Lab, March 5, 2021, <https://www.apmresearchlab.org/covid/deaths-by-race>.

⁹ See <https://www.npr.org/sections/health-shots/2020/05/27/862215848/across-texas-black-and-hispanic-neighborhoods-have-fewer-coronavirus-testing-sit> and <https://fivethirtyeight.com/features/white-neighborhoods-have-more-access-to-covid-19-testing-sites>.

¹⁰ Nambi Ndugga and others, "Latest Data on COVID-19 Vaccinations Race/Ethnicity" March 31, 2021, Kaiser Family Foundation, <https://www.kff.org/coronavirus-covid-19/issue-brief/latest-data-on-covid-19-vaccinations-race-ethnicity/>.

¹¹ Eric Morath, Theo Francis, and Justin Baer, "The Covid Economy Carves Deep Divide Between Haves and Have-Nots," The Wall Street Journal, October 5, 2020, <https://www.wsj.com/articles/the-covid-economy-carves-deep-divide-between-haves-and-have-nots-11601910595>.



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Hispanic or Latino (any race)	12.9	10.5	10.3	8.8	8.4	9.3	8.6	8.5	7.9
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Source: Bureau of Labor Statistics (BLS) Household Data Table A-2¹² and Table A-3,¹³ Seasonally adjusted. Note that categories overlap.

In a recent Pew Research Center survey, Black, Latino, and Asian American adults were significantly more likely than White respondents to report that they were struggling to pay their bills, had to use money from savings and retirement funds, had to borrow money from friends and family to make ends meet, had problems paying their rent or mortgage, or had lost health insurance coverage. For example, 43 percent of Black adults and 37 percent of Latino adults reported having trouble paying their rent or mortgage, while only 18 percent of White adults reported the same.¹⁴

C. A Plan to Preserve Homeownership, Particularly in Communities of Color

The health and economic effects of the pandemic will put people at risk of losing their homes and make it harder for them to enter or re-enter homeownership in the future. Loss of homeownership threatens the stability and vitality of all communities and disproportionately threatens Black, Latino, Indigenous, and Asian communities. But proactive policy changes can cushion the blow and even help communities build back more equitably.

A plan to preserve homeownership and protect neighborhoods now and into the future requires a coordinated effort across various policy levers. In this paper, we divide the policy changes into two categories: policies related to people and policies related to properties.

Chapter 2 (Impact of the COVID-19 Pandemic on People) describes the effect the pandemic has had on the ability of households to pay their mortgages and what this may mean for future foreclosures. It also describes the pandemic's effect on access to mortgage credit and provides a portrait of future homebuyers. We propose two broad strategies that will be critical for mitigating the impact of the pandemic on people: preventing foreclosures and ensuring access to sustainable and affordable credit.

Chapter 3 (Impact of the COVID-19 Pandemic on Properties) describes how our nation faces a housing shortage, especially of more affordable homes, despite strong home sales markets. We outline two strategies for confronting this problem: preserving and maintaining REO properties so they do not

¹² "Table A-2. Employment Status of the Civilian Population by Race, Sex, and Age," U.S. Bureau of Labor Statistics, April 6, 2021, <https://www.bls.gov/news.release/empsit.t02.htm>.

¹³ "Table A-3. Employment Status of the Hispanic or Latino Population by Sex and Age," U.S. Bureau of Labor Statistics, April 6, 2021, <https://www.bls.gov/news.release/empsit.t03.htm>.

¹⁴ Kim Parker, Rachael Minkin, and Jesse Bennett, "Economic Fallout from COVID-19 Continues to Hit Lower-Income Americans the Hardest," Pew Research Center Social & Demographic Trends, September 24, 2020, <https://www.pewsocialtrends.org/2020/09/24/economic-fallout-from-covid-19-continues-to-hit-lower-income-americans-the-hardest/>.



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deteriorate and prioritizing homeownership rather than rental when notes or foreclosed properties are sold.

Finally, the paper's conclusion briefly restates the challenges the pandemic poses to both people and properties and describes how we must chart a different course in our response to COVID-19 than we did in the aftermath of the Great Recession.

Chapter 2: The Impact of the COVID-19 Pandemic on People

It is widely recognized as a priority to ensure that the pandemic does not result in excessive or unnecessary foreclosures, which are bad for families because they are destabilizing, wealth stripping, and credit-ruining, and bad for neighborhoods because they reduce home values and cause blight. Policymakers should also aim to avoid excessive or unnecessary home loss as well, even when a homeowner has enough equity to sell without a deficiency, because any forced move (especially when they are geographically clustered) has similar negative effects on both households and communities.

A. Who Is Having Trouble Paying Their Mortgage During the Pandemic?

As of February 2021, more than two million borrowers (4.23 percent) were seriously delinquent on their mortgages, meaning they were more than 90 days past due or in the foreclosure process.¹⁵ This rate is more than five times the level seen before the pandemic. At 11.4 percent, the serious delinquency rate is highest for FHA borrowers who are disproportionately first-time homebuyers or households of color and is nearly the highest rate for FHA loans ever.¹⁶ In contrast, the serious delinquency rate is 2.78 percent on GSE loans (the Government Sponsored Enterprises—Fannie Mae and Freddie Mac).¹⁷

Low or negative equity elevates the risk that a loan will go into foreclosure. Data analytics firm Black Knight has estimated that 17 percent of FHA or VA loans in forbearance have less than 10 percent equity.¹⁸ However, only five percent of loans in forbearance held in bank portfolios or private-label securities (PLS) have less than 10 percent equity, and only four percent of GSE loans have less than 10 percent equity. The Urban Institute has estimated that among government-backed loans that are delinquent or in forbearance, less than one percent have negative equity and 5.5 percent have less than five percent equity.¹⁹ At the moment, negative equity does not appear to be a significant problem. However, as past-due amounts accumulate, borrowers who had little equity when they became delinquent will have even less.

¹⁵ "Black Knight February 2021 Mortgage Monitor," Black Knight, April 2020, https://cdn.blackknightinc.com/wp-content/uploads/2021/04/BKI_MM_Feb2021_Report.pdf.

¹⁶ "FHA Single Family Loan Performance Trends: February 2020 Credit Risk Report," U.S. Department of Housing and Urban Development, February 2020, https://www.hud.gov/program_offices/housing/hsgroom/loanperformance.

¹⁷ "Foreclosure Prevention Refinance and FPM Report Fourth Quarter 2020," Federal Housing Finance Agency, March 25, 2021, <https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/4Q2020FPR.pdf>.

¹⁸ "Black Knight August 2020 Mortgage Monitor," Black Knight, August 2020, https://cdn.blackknightinc.com/wp-content/uploads/2020/10/BKI_MM_Aug2020_Report.pdf.

¹⁹ Michael Neal and Laurie Goodman, "The Predicted Foreclosure Surge Likely Won't Happen, Even Among Financially Vulnerable Borrowers," February 11, 2021, <https://www.urban.org/urban-wire/predicted-foreclosure-surge-likely-wont-happen-even-among-financially-vulnerable-borrowers>.



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The states with the highest share of foreclosures or delinquent loans are Mississippi, Louisiana, Hawaii, Oklahoma, and Maryland.²⁰ States with significant numbers of loans with negative equity include Mississippi, Illinois, Iowa, and Connecticut.²¹ Metropolitan regions with significant concentrations of delinquent FHA loans, in particular, include Atlanta, Houston, and Chicago.²²

Public data on mortgage performance does not include the race or ethnicity of delinquent borrowers. Still, household surveys allow us to understand which categories of borrowers are having trouble making mortgage payments. While these surveys find different overall levels of hardship, each shows that Black and Latino homeowners are having the most difficulty paying their mortgage.

Fig. 2: Share of Households Having Trouble Paying Their Mortgage in Sept. 2020, by Race or Ethnicity

	Total	White	Black	Hispanic	Asian
Census Pulse Survey (Share not currently caught up on mortgage payment)	9.8%	7.0%	19.4%	17.0%	13.0%
Understanding America Survey (Share that missed or delayed mortgage payment in the past month)	6.2%	5.1%	5.9%	11.9%	4.0%

Source: Urban Institute, "Measuring the Crisis: Housing Data during the COVID-19 Pandemic"²³

B. Background: CARES Act Forbearance

The economic and health impacts of the COVID pandemic could push a large number of homeowners into foreclosure or a forced sale. Fortunately, decisive action from the federal government has so far protected homeowners. But whether these outcomes are truly prevented or merely delayed depends on how our economy performs in the coming months, as well as whether the mortgage servicing industry can help homeowners get back on track and whether the federal government provides additional support to troubled borrowers.

To mitigate negative consequences for the economy, Congress passed the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") in March 2020.²⁴ For the single-family mortgage market, Section 4022 of the CARES Act gives borrowers with federally-backed (FHA, VA, USDA, Fannie Mae, or Freddie Mac) mortgages the right to a "forbearance"—the ability to pause mortgage payments for a specific period—if they are affected by a COVID-related hardship. The CARES Act also established a foreclosure moratorium for federally-backed mortgages.

²⁰ "Black Knight February 2021 Mortgage Monitor."

²¹ "Homeowner Equity Insights: Data through Q4 2020," CoreLogic, 2021, <https://www.corelogic.com/insights-download/homeowner-equity-report.aspx>.

²² Ed Pinto and Tobias Peter, "Nowcast: 10 Metros Most Threatened by High Numbers of FHA Delinquencies," American Enterprise Institute, October 2020, <https://www.aei.org/nowcast-10-metros-most-threatened-by-high-numbers-of-fha-delinquencies-october-2020-update/>.

²³ "Measuring the Crisis: Housing Data during the COVID-19 Pandemic," Urban Institute, October 26, 2020, <https://www.urban.org/events/measuring-crisis-housing-data-during-covid-19-pandemic>.

²⁴ See <https://www.congress.gov/116/plaws/publ136/PLAW-116publ136.pdf>.



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When borrowers request forbearance from their mortgage servicer, they simply need to attest to having a COVID-related hardship and do not need to provide any documentation. They may request forbearance whether or not they are current on their mortgage. Additionally, the CARES Act prohibits servicers from charging late fees or other penalties and provides some protection against negative credit reporting to credit bureaus. However, the payments paused during forbearance are not forgiven; the borrower will still owe the arrearages (past due amounts). Consequently, after forbearance ends, borrowers must work with their servicers to determine how the loans will be repaid.

About 70 percent of the mortgage market is federally backed and therefore entitled to these forbearance protections. The remainder of loans in the market are either in bank portfolios or in private-label securities. While the CARES Act did not protect borrowers with these types of loans, many servicers are voluntarily offering similar forbearance options to these borrowers, although they do not necessarily offer the same number of months or the same post-forbearance options.

C. Are Households of Color Taking Advantage of Mortgage Forbearance?

Currently, about 2.7 million homeowners are on a forbearance plan, down from a peak of about 4.8 million in May 2020.²⁵ About 1.1 million of these homeowners have FHA or VA loans, 930,000 have GSE loans, and the remaining are portfolio loans or in private-label securities. Most borrowers in forbearance are seriously delinquent, but about a quarter of those in forbearance remain current on their mortgage.²⁶ While the number of borrowers in forbearance began declining in early June 2020, since early November 2020, the number of borrowers in forbearance has remained relatively stable.²⁷

Many households never entered forbearance despite falling behind on their mortgage. Seventeen percent (386,000) of post-COVID delinquencies and 39 percent (412,000) of pre-COVID delinquencies are not in active loss mitigation and have not entered a forbearance plan.²⁸

Data points concerning equitable access to forbearances are mixed right now. Data from both GSEs show that among households with a post-March 1, 2020, mortgage delinquency, a higher share of Black, Latino, and Asian households have entered forbearance than non-Hispanic White borrowers.²⁹ (Critically, however, we do not have similar data for FHA borrowers.) On the other hand, the Urban Institute has found that predominantly Black or Latino neighborhoods have nearly double the share of delinquent borrowers who are not in forbearance as predominantly White zip codes.³⁰

So far, forbearance appears to be one of the few government success stories of the pandemic. A recent study by JP Morgan Chase used checking account data to examine the impact of forbearance on the

²⁵ "Black Knight February 2021 Mortgage Monitor."

²⁶ "Black Knight September 2020 Mortgage Monitor," Black Knight, September 2020, https://cdn.blackknightinc.com/wp-content/uploads/2020/10/BKI_MM_Sept2020_Report.pdf.

²⁷ "Black Knight February 2021 Mortgage Monitor."

²⁸ "Black Knight February 2021 Mortgage Monitor."

²⁹ Malloy Evans and Steve Holden, "Getting Hope to Where it is Needed Most," Fannie Mae, October 16, 2020, <https://www.fanniemae.com/research-and-insights/perspectives/getting-help-where-its-needed-most>. Kevin Palmer, "Our Work During COVID has Helped Families Keep their Homes," Freddie Mac, October 16, 2020, http://www.freddiemac.com/perspectives/kevin_palmer/20201016_our_work_during_covid.page.

³⁰ Michael Neal and Caitlin Young, "Delinquent Homeowners in Neighborhoods of Color Are Less Likely to Be Protected by Forbearance," Urban Institute, December 2, 2020, <https://www.urban.org/urban-wire/delinquent-homeowners-neighborhoods-color-are-less-likely-be-protected-forbearance>.



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household finances of its mortgage customers and found that forbearance helped families maintain their cash buffers.³¹ In addition, Chase found minimal evidence of borrowers taking advantage of forbearance when there is no apparent need. Families in forbearance were more likely to have lost labor income and received unemployment benefits than families not in forbearance. Families using forbearance to miss mortgage payments had larger drops in income than other homeowners.

D. How Do Borrowers Fare When Exiting Forbearance?

Fifty-nine percent of borrowers who have been in forbearance have exited.³² When borrowers exit forbearance, they must work with their servicer to determine how to pay back any arrearages accumulated during that time.

The Mortgage Bankers Association reports that of borrowers exiting forbearance between June 1, 2020, and April 18, 2021, about half were able to reinstate their mortgages right away—25.4 percent never missed a payment while in forbearance, 14.4 percent were able to repay all past-due amounts at once, and 7.5 percent paid off their mortgage through a refinance or by selling the home.³³ However, the remainder needed assistance to make up their missed mortgage payments. Twenty-seven percent of borrowers arranged to pay these amounts by putting the arrearages into a balloon payment at the end of their mortgages through a deferral or partial claim. In comparison, 9.6 percent received a loan modification that amortizes the missed payments over the loan term. Finally, and most concerning, 14.6 percent exited forbearance without a plan in place for making up their missed payments; these loans remain delinquent and will proceed to foreclosure if the borrowers do not make arrangements with their servicers.

In contrast, Black Knight estimates that about eleven percent of borrowers exited forbearance without a payment plan in place. Of these, 7 percent (306,000) are currently negotiating loss mitigation with their servicer, but four percent, or about 167,000 borrowers, are delinquent and not pursuing loss mitigation.³⁴ Without intervention, these loans also will be at significant risk of foreclosure.

One additional reason for concern is that it is likely that the borrowers who will have the hardest time resuming their mortgage payments and making up missed payments have remained in forbearance, rather than exiting forbearance before reaching the maximum forbearance term.

E. How Much Risk Does the Mortgage Market Face Now?

Fortunately, the mortgage market is in a much better place going into this crisis than going into the Great Recession. In large part, due to protections put in place through the Dodd-Frank Act, significantly fewer borrowers have the types of high-risk mortgage loans that failed in substantial numbers during the last recession. Additionally, the share of borrowers with less than 10 percent equity

³¹ "Did Mortgage Forbearance Reach the Right Homeowners?," JP Morgan Chase & Co., December 2020, <https://www.jpmorganchase.com/institute/research/household-debt/report-did-mortgage-forbearance-reach-the-right-homeowners>.

³² "Black Knight October 2020 Mortgage Monitor."

³³ "Share of Mortgage Loans in Forbearance Declines to 4.49 Percent," Mortgage Bankers Association, April 26, 2021, <https://www.mba.org/2021-press-releases/april/share-of-mortgage-loans-in-forbearance-slightly-decreases-to-449>.

³⁴ "Black Knight February 2021 Mortgage Monitor."



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when the pandemic began (6.6 percent) is less than half what it was entering 2007 (14.5 percent).³⁵ As we describe further in Chapter 3, the current home prices and home sales strength also helps mitigate risks to the housing market.

Additionally, the pandemic's effect on consumer finances overall has not been as negative as one might expect, partly due to income support provided by the federal government through enhanced unemployment insurance and direct stimulus payments. Throughout the pandemic, consumers have saved more and paid down debt.³⁶ The average FICO score has increased five points to 711.³⁷

That said, even in the best-case scenario, the crisis could result in more home losses and foreclosures (maybe significantly more) compared to pre-COVID levels. ATTOM Data projected in July 2020 that anywhere from about 225,000 to 500,000 homeowners throughout the country could face foreclosure throughout 2021.³⁸ Andy Davidson & Company expects REO inventory to peak in the third quarter of 2024 at about 175,000 foreclosures brought to auction, which is double the pre-pandemic level, but about 40 percent below the Great Recession peak.³⁹

F. Declining Mortgage Credit Availability Due to COVID-19-Related Policy Changes

Before COVID-19, even as the credit box widened somewhat, mortgage credit had never bounced back to pre-financial crisis levels, even for safe products.⁴⁰ Data show that due to COVID-19, mortgage credit has returned to tightening both for FHA and GSE originations.⁴¹ Among FHA endorsements, in particular, there has been a shift toward higher credit score borrowers. More generally, there has been an uptick in average credit scores for purchase and refinance loans. In February 2021, Ellie Mae reported that the average FICO score on all closed loans for the month was 753, compared to 738 at the start of 2020.⁴² Overall originations have been growing for both home purchase loans and refinance; 68 percent of all closed loans in February 2021 were refinanced loans compared to 50 percent in January 2020.⁴³ However, much of this increase was driven by higher-balance loans that are

³⁵ "February 2020 COVID-19: Potential Impact on Mortgage Performance," Black Knight, February 2020, https://cdn.blackknightinc.com/wp-content/uploads/2020/04/BKI_MM_Feb2020_Report.pdf.

³⁶ Stacy Cowley, "Recession's Silver Lining: American Households Are Doing Better than Expected," New York Times, Oct. 27, 2020, <https://www.nytimes.com/2020/10/27/business/recession-consumers-savings.html>.

³⁷ Ethan Dornhelm, "Average U.S. FICO Score at 711, But Uncertainty Abounds," FICO Blog, October 19, 2020, <https://www.fico.com/blogs/average-us-fico-score-711-uncertainty-abounds>.

³⁸ "Residential Foreclosure Activity in U.S. Could Easily Double Over Coming Year," ATTOM Data Solutions, July 31, 2020, <https://www.attomdata.com/news/market-trends/figuresfriday/residential-foreclosure-activity-in-u-s-could-easily-double-over-coming-year/>.

³⁹ "Housing and Foreclosure Market Trends," Auction.com, September 2020,

<https://www.dropbox.com/s/qzilympp1hh5un7/Auction.com%20Market%20Insights%20Presentation%20-%20NCST.pdf?dl=0>; "Q4 2020 Distressed Market Outlook," Auction.com, November 2020, <https://www.auction.com/lp/in-the-news/2021-distressed-market-outlook/>.

⁴⁰ Urban Institute, "Housing Credit Availability Index," January 2021, <https://www.urban.org/policy-centers/housing-finance-policy-center/projects/housing-credit-availability-index>.

⁴¹ Michae Neal, Linna Zhu, and Faith Schwartz, "During the Pandemic, Policymakers Should Maintain Forbearance but Fix Its Costs," Urban Institute, September 2020, https://www.urban.org/sites/default/files/publication/102891/during-the-pandemic-policymakers-should-maintain-forbearance-but-fix-its-costs_0.pdf.

⁴² "February 2021 Origination Insight Report," Ellie Mae, February 2021, https://static.elliemae.com/pdf/origination-insight-reports/ICE_OIR_FEB2021.pdf.

⁴³ Ibid.



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more likely taken out by high-income households.⁴⁴ Tightening of mortgage credit is likely to have a disparate impact on households of color, who tend to have lower credit scores and live in communities with fewer bank branches and mortgage brokers.

Who Are the Homebuyers of the Future?

The Urban Institute recently projected that between 2020 and 2040, all net new homeowners will be households of color,⁴⁵ and absent policy changes, the overall homeownership rate will drop from 65 to 62 percent. Homeownership rates will drop among both White and Black households. Seventy percent of net new homeowners will be Latino, who tend to be younger, have less income and wealth and lower credit scores, and are more likely to be in intergenerational households than White families.⁴⁶

In 2020, millennials made up the largest share of homebuyers, at 38 percent,⁴⁷ and will continue to drive the market. That said, while an average of 34 percent of millennials in the largest metropolitan areas are mortgage-ready, only 20 percent of Black and 28 percent of Latino millennials are mortgage-ready.⁴⁸

To serve the homebuyers of the future with affordable and sustainable credit, policymakers and the mortgage industry must make progress on several fronts, including:

- Providing down payment assistance to socially or economically disadvantaged households, such as those who are first generation homebuyers;
- Increasing the availability of small-balance mortgages (such as those with balances below \$75,000), which are critical for low- and moderate-income families to purchase low-cost homes;
- Combatting the trend of excessive risk-based pricing among lenders and the GSEs, which raises the cost of mortgages for those who can least afford it; and
- Exploring innovations in consumer credit scoring, including by incorporating non-traditional data.

One largely untapped opportunity for lenders and secondary market players is to expand the origination and purchase of loans made under Special Purpose Credit Programs, which are allowable

⁴⁴ "Mortgage Applications Decrease in Latest MBA Weekly Survey," Mortgage Bankers Association, September 30, 2020, <https://www.mba.org/2020-press-releases/september/mortgage-applications-decrease-in-latest-mba-weekly-survey-x272988>.

⁴⁵ Laurie Goodman and Jun Zhu, "The Future of Headship and Homeownership," Urban Institute, January 2021, available at <https://www.urban.org/research/publication/future-headship-and-homeownership>.

⁴⁶ Ibid.

⁴⁷ "2020 Home Buyers and Sellers Generational Trends Report," National Association of REALTORS[®] Research Group, March 2020, <https://www.nar.realtor/sites/default/files/documents/2020-generational-trends-report-03-05-2020.pdf>.

⁴⁸ Mortgage-ready millennials are those under 40 with strong enough credit to qualify for a mortgage (a FICO score of 620 or above, a debt-to-income ratio of 25 percent or less, and no recent foreclosures, bankruptcies, or serious delinquencies). Following NAR's methodology, a home is affordable if a consumer's quarterly household income is greater than or equal to the annual mortgage payment on a median priced house (under the assumption of 10 percent down payment, 4 percent mortgage rate, and 30 year contract). Laurie Goodman, Sarah Stochak, and Jaya Dey, "More than 19 Million Millennials in 31 US Cities Are Ready to Become Homeowners," Urban Institute, September 26, 2018, <https://www.urban.org/urban-wire/more-19-million-millennials-31-us-cities-are-ready-become-homeowners>.



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under the Equal Credit Opportunity Act. These lending products are designed to provide opportunities for economically disadvantaged consumers to obtain quality, sustainable mortgage financing.⁴⁹

G. Recommendations

To address these issues, we recommend two primary strategies:

1. Prevent foreclosures:

- a. Increase access to COVID mortgage forbearances;
- b. Give borrowers the post-forbearance option best suited for their circumstances;
- c. Encourage communication between borrowers and mortgage servicers;
- d. Ensure the Homeowner Assistance Fund meets its goals; and,
- e. Support alternatives to foreclosure for those who need them.

2. Ensure that households can access affordable and sustainable mortgage credit:

- a. Prevent the pandemic from negatively affecting consumer credit scores;
- b. Allow borrowers to access new mortgages after forbearance and foreclosure; and,
- c. Eliminate forbearance penalties that decrease access to credit.

PREVENT FORECLOSURES

Helping homeowners avoid unnecessary home loss, and especially foreclosure, whenever possible is critical for the health of individuals, neighborhoods, and the economy. The effects of home loss and foreclosure include significant financial loss for homeowners, housing instability, loss of quality community benefits, and in some cases, increased family separation, including divorce.⁵⁰ The adverse effects of eviction and displacement for households are substantial. Foreclosures also destabilize neighborhoods, causing the value of neighboring homes to fall and negatively impacting local housing markets. Vacant properties cost local governments in lost property tax revenue and increased expenses to fight crime and health hazards. Foreclosures are also costly for mortgage investors.

These recommendations are designed to prevent unnecessary home loss and foreclosure.

1. Increase Access to COVID Mortgage Forbearances

Currently, only borrowers in federally-backed mortgages are protected by CARES Act forbearances or by federal foreclosure moratoria.⁵¹ That leaves borrowers in private mortgages—about 30 percent of the market—without formal protections. Congress should add private borrowers to the CARES Act protections, and regulators should encourage banks and mortgage servicers to extend these protections even if not legislated by Congress.

⁴⁹ Lisa Rice, “Using Special Purpose Credit Programs to Expand Equality,” National Fair Housing Alliance, November 4, 2020, <https://nationalfairhousing.org/using-spcps-blog/>.

⁵⁰ Sharada Dharmasankar and Bhash Mazumder, “Have Borrowers Recovered from Foreclosures during the Great Recession?,” Chicago Federal Reserve, 2016, <https://www.chicagofed.org/publications/chicago-fed-letter/2016/370>.

⁵¹ Some states also have their own foreclosure moratoria.



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Several surveys have found that many borrowers with federally-backed mortgages are unaware of the CARES Act mortgage protections.⁵² While some federal agencies have added information about forbearance and post-forbearance to their websites, and a group of industry representatives and consumer advocates has stepped up to create a voluntary campaign to reach borrowers,⁵³ these efforts do not take the place of a formal campaign. To reach these borrowers, we recommend a government-wide outreach campaign to educate borrowers about forbearance options run not just in conjunction with the CFPB, HUD, and FHFA but also through all government agencies that interact with homeowners in need (such as public benefits programs).

2. Give Borrowers the Post-Forbearance Option Best Suited for Their Circumstances

Congress has not defined the options that borrowers are to be offered when exiting forbearance,⁵⁴ leaving it up to federal agencies and private investors to determine post-forbearance options for borrowers. As a result, these options have not been standardized across the market. We recommend that Congress require all mortgage servicers to offer post-forbearance options that do not require arrearages to be repaid in a lump sum and that do not increase the borrower's monthly payments, subject to a safe harbor for situations in which the servicers cannot do so under the terms of their pooling and servicing agreement. It is also important that servicers make available streamlined options that do not require burdensome documentation requirements.

FHA and the GSEs generally refer to their loss mitigation options according to a "waterfall." Under this construct, servicers evaluate borrowers for the first option in the waterfall before evaluating borrowers for the second, third, fourth option, and so forth. An issue may arise when a borrower qualifies for and accepts an earlier option in the waterfall when a later option is more suitable for that borrower.⁵⁵ To address this, we recommend that FHA, the GSEs, and other investors clarify that servicers should tell a borrower what all their options are before deciding on each option individually. For example, when a servicer asks a borrower if they can resume their pre-COVID payment through a deferral or partial claim and does not mention that there are other options, many borrowers will say yes even if they

⁵² "Forbearance and Delinquency Summary of Housing Counselor Survey," National Housing Resource Center, July 20, 2020, <https://www.hsgcenter.org/wp-content/uploads/2020/07/Survey-results-Forbearance-and-Delinquency2.pdf>.
Douglas Duncan, "COVID-19: The Need for Consumer Outreach and Home Purchase/Refinance Digitization," Fannie Mae, August 12, 2020, <https://www.fanniemae.com/research-and-insights/perspectives/covid-19-need-consumer-outreach-and-home-purchasefinancing-digitization>.

⁵³ Materials are available at www.covidhelpforhome.org.

⁵⁴ There are a range of tools that assist homeowners who are behind on their payments in getting back on track:

- Repayment plan: If a homeowner can afford to pay more than their previous payment, they can repay the missed amount over time.
- Payment deferral (GSE) or partial claim (FHA): This option allows households to resume making their pre-COVID payment by deferring the missed payments to the end of the loan. That amount will become due when the loan is refinanced, at the end of the loan term, or when the house is sold.
- Loan modification: This option changes one or more terms of the loan to bring the loan current. Such changes can include interest rate reduction, term extension, deferral or forgiveness of principal and past due amount, or any combination thereof. A modification can be temporary, such as lowering the interest rate for a limited time period, or permanent. Long-term affordable permanent loan modifications offer the best opportunity to ensure that the borrower does not redefault.

⁵⁵ In both the GSEs and FHA waterfalls, a borrower is evaluated for a payment deferral (GSE) or partial claim (FHA) before he or she is evaluated for a loan modification. It is possible that some borrowers are ending up in payment deferrals, which keep a borrower's payments the same, when they have in fact lost income and a loan modification that reduces their payment would be more appropriate.



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cannot afford it, because they think their only other option is to lose the home. But if a servicer lets a borrower know up front that there will be several options and that they should choose the option they can afford, it's more likely the borrower will end up in a sustainable post-forbearance solution.

Another obstacle for borrowers with GSE loans is that the GSEs' Flex Modification ("Flex Mod") option does not reduce the borrower's interest rate to the current market rate if they have more than 20 percent equity in their home, as a very high percentage of GSE borrowers do. This structure significantly reduces the likelihood that the modification will lower a borrower's payments substantially. Their stated view is that if a borrower has more than 20 percent equity, they can sell their home without requiring a short sale. However, as we have noted throughout this paper, the best solution for both families and communities is to avoid home loss even when it's not through a short sale or foreclosure. Thus, we recommend that the Federal Housing Finance Agency ("FHFA") and the GSEs allow borrowers who have more than 20 percent equity in their homes to access interest rate reductions as part of a Flex Mod.

One encouraging development is that FHA has made borrowers who were delinquent before the COVID crisis eligible for the same streamlined options as borrowers who became delinquent during the pandemic. However, FHA needs to clarify its rules to ensure that these borrowers have the same access to loss mitigation, including allowing servicers to capitalize certain advances they made to cover expenses related to these borrowers into payment deferrals or loan modifications. FHA should also consider requiring servicers to waive late fees for all borrowers, including those who were delinquent before the crisis.

Also, FHA's modification programs do not currently allow a servicer to offer a modification with a term of 40 years. However, extending the loan term to 40 years may be necessary to sufficiently reduce a borrower's payment, especially as interest rates rise. FHA should consider permitting servicers to offer the option of modifications with 40-year terms, which FHA did in a limited way right after the financial crisis and which would align with the GSE's Flex Mod.

Finally, many borrowers will exit forbearance with shortages in their escrow accounts, which servicers use to pay taxes and insurance on behalf of the borrower. These shortages cannot be deferred in a payment deferral or included in a Flex Mod for borrowers with GSE loans. We encourage the GSEs to change this policy. In addition, servicers are not required to perform escrow analyses, which predict whether a borrower will have a shortage when borrowers exit forbearance or enter payment deferrals. However, doing so is an extremely good practice. We also recommend that servicers give borrowers who need time to repay these amounts the flexibility they need.

3. Encourage Communication Between Borrowers and Mortgage Servicers

During the foreclosure crisis, the mortgage servicing industry was completely unprepared for the volume of requests from borrowers experiencing difficulty paying their mortgages. It is critical servicers are prepared and adequately staffed to meet the surge in demand from borrowers that will occur when they reach the end of their forbearance periods to avoid repeating a similar scenario. Doing so requires training front-line staff, implementing internal oversight and quality control measures, collecting and reporting detailed data about borrower demographics and loss mitigation outcomes, and providing additional services to borrowers who need them, such as language services for those with limited English proficiency.



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Another critical ingredient is support for and oversight of mortgage servicers by regulatory agencies. The success of the forbearance and post-forbearance regime will depend largely on the ability of servicers to execute well – to make quality right party contact and communicate clearly with borrowers. We recommend that regulators, including the CFPB, FHFA, OCC, FDIC, the Federal Reserve, FHA, VA, and USDA, closely monitor servicing performance, as the CFPB has recently announced it will do.⁵⁶ To monitor performance, regulators need to collect quality data about loss mitigation outcomes and ensure that servicers train their staff and closely monitor their performance. That data should also be made available to the public and academic and nonprofit researchers.

We further recommend that CFPB, potentially in collaboration with other government agencies, publish standardized talking points, scripts, and model templates and letters for communicating with borrowers about forbearance and loss mitigation. To ensure that these documents are as clear and concise as possible, we recommend CFPB develop them with input from housing counselors, fair housing organizations, legal aid attorneys, and others who specialize in communicating with borrowers about mortgage servicing.

Along those lines, any effort to improve communication between borrowers and servicers should recognize the importance of trusted helpers such as housing counselors, fair housing practitioners, and legal aid attorneys. Even the clearest servicer communications will still require borrowers to consider difficult trade-offs, such as the implications of having a balloon payment at the end of their mortgage, using up their partial claim, or a term extension, and mortgage servicer call center staff are generally not in a position to advise borrowers on their financial choices beyond a determination of affordability. Servicers should seek to design processes that encourage collaboration with these intermediaries as much as possible. Because one limiting factor on the use of counselors or attorney advisors is their availability, as the intermediary sector is perennially resource-constrained, Congress and agencies should ensure that these intermediaries receive the funds needed to meet the pandemic-related needs.

Concurrent with these other steps, we should revisit how servicers are compensated for their work. Reform of servicing compensation that aligns the incentives of servicers with those of homeowners and investors could significantly improve servicer practices by encouraging them to invest directly in activities that help homeowners. While a complete overhaul of mortgage servicing compensation will be a long-term process, investors such as Fannie Mae and Freddie Mac routinely provide incentive payments to servicers for completing certain alternatives to foreclosure. Other investors should assess whether similar incentives could improve outcomes for homeowners and their bottom lines.

The CFPB recently proposed a pre-foreclosure review period (essentially a foreclosure moratorium) through the end of 2021 for primary residences in an effort to encourage loss mitigation.⁵⁷ Because a foreclosure moratorium alone does not provide any new incentive for borrowers who are not already in contact with their servicer to do so, and because the longer borrowers wait, the more difficult it will be

⁵⁶ Consumer Financial Protection Bureau, “Bulletin 2021-02: Supervision and Enforcement Priorities Regarding Housing Insecurity,” https://files.consumerfinance.gov/f/documents/cfpb_bulletin-2021-02_supervision-and-enforcement-priorities-regarding-housing_WHcae8E.pdf.

⁵⁷ Consumer Financial Protection Bureau, “CFPB Proposes Mortgage Servicing Changes to Prevent Wave of COVID-19 Foreclosures,” April 5 2021, <https://www.consumerfinance.gov/about-us/newsroom/cfpb-proposes-mortgage-servicing-changes-to-prevent-wave-of-covid-19-foreclosures/>.



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to get them into an affordable loss-mitigation solution that allows them to keep their home, we support CFPB creating exceptions, which the agency calls “off ramps,” as long as the off-ramps drive meaningful loss mitigation. Specifically, we recommend an off-ramp for servicers to permit them to initiate a foreclosure before December 31 where they have proactively offered a borrower for a streamlined payment reduction modification, and the borrower did not take it. For any borrowers who are not eligible for loss mitigation, servicers should provide written denial notices that explain why they are not eligible and enable borrowers to appeal that denial if there has been servicer error.

Effective off-ramps are also important to prevent neighborhood blight. If servicers do not provide loss mitigation to the vast majority of delinquent borrowers in a timely manner, we risk overwhelming the foreclosure system with hundreds of thousands of foreclosure filings, a situation which significantly contributed to blight after the financial crisis. The CFPB rule should explicitly consider how to avoid this foreclosure cliff. Also, the CFPB should include an off-ramp for vacant and abandoned properties that is specific and clear enough that servicers will use it (some servicers are not using the existing vacancy exception to current moratoria for fear of getting it wrong). Indeed, all of the off-ramps will need to have very clear instructions for when servicers can proceed with foreclosures so the servicers don't simply play it safe and wait for the expiration of the pre-foreclosure period.

4. Ensure the Homeowner Assistance Fund Achieves Its Goals

Congress recently created a \$9.9 billion Homeowner Assistance Fund to provide direct assistance to homeowners who are having trouble paying their mortgages or keeping up with other housing-related expenses, such as property taxes, property insurance, and utilities. The fund is modeled after the Hardest Hit Fund that provided similar assistance following the Great Recession. The fund will be administered by state HFAs, territories, and tribes (henceforth states) according to guidance promulgated by Treasury.

The creation of the Homeowner Assistance Fund will be a critical lifeline to borrowers who are not well served by existing loss mitigation programs, including borrowers who are not covered by the CARES Act, who are in danger of tax foreclosure rather than mortgage foreclosure, whose incomes are not restored fully, or who cannot qualify for a deferral or loan modification without an additional cash contribution. However, whether the Homeowner Assistance Fund can live up to its promise depends on how Treasury and states implement it and whether mortgage servicers fully embrace it.

A \$9.9 billion fund is smaller than what is needed to meet the full spectrum of needs of struggling mortgage borrowers, and Congress should be ready to allocate additional funds if necessary. At the same time, we believe from the experience of the Hardest Hit Fund that there is a considerable risk that states will not spend their Homeowner Assistance Funds quickly enough. It is critical that Treasury and states avoid restrictive program requirements, address program bottlenecks, and work proactively to provide funds to borrowers who could benefit from them.

To achieve the Homeowner Assistance Fund's full promise, we recommend that Treasury and the states create as standardized a system as possible, especially in terms of household eligibility requirements and the process flows of programs that interact with mortgage servicers and other multi-state stakeholders. Additionally, they should give homeowners flexibility in documenting their hardship, income, and additional information.



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The HAF should also allow homeowners to access funds through multiple mechanisms, including when their servicer identifies that the homeowner would benefit from assistance when a borrower proactively requests help and when a housing counselor or legal services provider requests funds on a homeowner's behalf. Prioritizing equity for the hardest hit homeowners and communities, especially communities of color, is also a critical goal and requires thoughtful planning to target those communities and help borrowers quickly and efficiently.

5. Support Alternatives to Foreclosure for Borrowers Who Need Them

While all home loss imposes costs both on families and neighborhoods, inevitably, some borrowers who have not been able to regain their financial footing will no longer be able to sustain their mortgage even with a loan modification. Borrowers who cannot qualify for a home retention option should be encouraged to exit the home through a sale, short sale, or deed-in-lieu of foreclosure (sometimes called "cash for keys"), lessening damage to their credit and allowing them to re-enter homeownership more quickly than if they went through foreclosure. For homeowners with equity, a sale could avoid the possible loss of equity if the property is sold at foreclosure. For investors, these options are usually less expensive and more efficient than taking the borrower through the foreclosure process.

We recommend four strategies to encourage the use of these tools:

- **Borrower Education:** Servicers and other real estate professionals should educate borrowers about the potential benefits of listing their home for sale rather than going through foreclosure. Borrowers who cannot afford to sustain their current home may not realize that a difficult and potentially expensive foreclosure will eventually occur. Helping borrowers understand their options and the consequences can help borrowers make the best decision for their circumstances.
- **Time to Market Property:** Servicers should allow homeowners sufficient time to market their property, whether as a normal home sale or a short sale, to avoid foreclosure.
- **Quick Response:** FHFA, FHA, VA, and USDA should ensure that their short sale rules prioritize quick action, whether through delegated authority to servicers or another mechanism. Short sales are most likely to fail when approvals or denials do not come quickly.
- **Relocation Expenses:** For homeowners who cannot obtain a home retention option but are reluctant to engage other alternatives to foreclosure, servicers should provide monetary incentives or relocation expenses to struggling homeowners to participate in short sale or deed-in-lieu transactions. Fannie Mae, Freddie Mac, and FHA each provide up to \$3,000 for borrower relocation expenses following short sales or deed-in-lieu transactions. Other investors should consider providing similar or larger levels of assistance.

ENSURE THAT HOUSEHOLDS CAN ACCESS AFFORDABLE AND SUSTAINABLE MORTGAGE CREDIT

1. Prevent the Pandemic From Negatively Affecting Consumer Credit Scores

An important way to help position consumers to re-enter homeownership when they are ready is to put policies in place that do not unduly penalize borrowers affected by the pandemic. Given the dire effects of the health and economic crises, borrowers accessing forbearance, foreclosure moratoria, loan modifications, short sales, deeds in lieu of foreclosure, and other options should experience *de minimis*



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impact to their credit profiles. Policymakers should adopt credit-related guidelines to ensure consumers affected by the pandemic will recover; this will benefit individuals and help boost the overall economy.

Sound credit scoring policies are essential from a racial equity perspective as well. Because of deep inequities that existed prior to the COVID-19 pandemic, communities of color are more vulnerable to its effects. Even before the crisis hit, the racial wealth and homeownership gaps were growing, and borrowers of color were positioned unfavorably. A disproportionate percentage of Black and Latino borrowers were either credit invisible or had lower credit scores than their White counterparts.⁵⁸ These inequities exist because these consumers have historically been precluded from passing on wealth to subsequent generations,⁵⁹ disproportionately live in credit deserts,⁶⁰ and have access to credit only from non-traditional financial service providers.⁶¹

At a minimum, furnishers of credit data should carefully monitor how they report forbearances, loan modifications, and short sales to the credit bureaus, including their use of special comment codes. How these foreclosure avoidance strategies are reported to credit bureaus can have different impacts on a consumer's credit score. Furnishers of credit information should also take care not to report consumers as delinquent after forbearance while the consumer is negotiating loss mitigation.

Finally, the largest housing-related danger to credit scores is likely to be debt collection efforts for unpaid rent. Damaging the credit scores of today's struggling tenants will only further delay their entry into homeownership. We encourage Congress to consider banning debt reporting for unpaid rent arrearages related to COVID hardships.

2. Allow Borrowers to Access New Mortgages After Forbearance and Foreclosure

Both the GSEs and FHA should revamp their policies to allow borrowers who took advantage of the CARES Act forbearance program to move to a new home or gain access to lower-priced mortgages through a refinance. Currently, both FHA and FHFA require borrowers who have been in forbearance to make timely mortgage payments for at least three months after exiting forbearance before they can get a new loan to purchase or refinance a home.⁶² This lockout applies unless the borrower has fully reinstated the mortgage—to make full repayment of all missed payments—immediately. Certain FHA loans may require six (streamlined) or even 12 (cash-out) consecutive monthly payments before refinancing is allowed.

⁵⁸ Alanna McCargo and Jung Choi, "Closing the Gaps: Building Black Wealth Through Homeownership," Urban Institute, December 2020, https://www.urban.org/sites/default/files/publication/103267/closing-the-gaps-building-black-wealth-through-homeownership_0.pdf.

⁵⁹ Emanuel Nieves, "The Road to Zero Wealth: How the Racial Wealth Divide is Hollowing Out America's Middle Class," Prosperity Now, September 14, 2017, <https://prosperitynow.org/blog/new-report-finds-racial-wealth-inequality-growing-national-emergency>.

⁶⁰ Cheryl Young and Felipe Chacon, "50 Years After the Fair Housing Act Inequality Lingers," Trulia, April 19, 2018, <https://www.trulia.com/research/50-years-fair-housing/>.

⁶¹ "Access to Credit," National Fair Housing Alliance, November 2020, <https://nationalfairhousing.org/access-to-credit/>

⁶² See Fannie Mae Lender Letter LL 2020-03 (Updated November 13, 2020); Freddie Mac Bulletin 2020-17, "Selling Guidance Related to COVID-19" (reissued May 22, 2020); FHA Mortgage Letter 2020-30 (September 10, 2020).



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For some borrowers, selling their home and downsizing to a more affordable option is the best path forward. But under current policies, these borrowers will not be able to access GSE financing until at least three months after their forbearance ends if they have taken advantage of a loss mitigation solution, thereby limiting their ability to pursue this path. For FHA financing, this temporary prohibition on new credit applies to all borrowers who elected not to make payments during their forbearance. We encourage FHA and the GSEs to lift these policies and other investors to avoid them.

For some borrowers, particularly those whose incomes do not return to their full pre-COVID levels, refinancing may offer the best option for holding onto their homes with an affordable, and hence sustainable, mortgage payment. Current mortgage interest rates, which may be as little as 3.2 percent, are close to historic lows, even though they have increased since 2020. Providing these borrowers with the ability to refinance their mortgages at a new, low interest rate may be the best way to help them keep their homes and sustain their mortgage payments.

Following a foreclosure sale, a borrower is generally ineligible for a new mortgage loan for three (FHA) to seven (GSE) years. We recommend that these policies be reconsidered. Given the time-limited nature of the pandemic, a borrower's loss of their home through foreclosure may not be a strong predictor of their future ability to sustain homeownership. A possible blueprint for policy change is FHA's now-expired Back to Work program, which allowed a borrower to qualify for a FHA loan sooner if they completed housing counseling and could show that the economic hardship that caused their foreclosure had been resolved.

3. Eliminate Forbearance Penalties That Decrease Access to Credit

During the pandemic, both FHA and FHFA put temporary policies in place to permit the endorsement or delivery of a mortgage that went into forbearance after closing, but these policies have expired.

To avoid a situation where they need to hold loans originally intended for FHA or the GSEs, lenders (especially those without portfolio capacity) have grown more cautious in their lending, leading to a contraction in mortgage credit availability. These policies have further reduced access to credit for borrowers of color and those living in communities hardest hit by the coronavirus. They also contradict the countercyclical role that these entities were created to provide and played during the last crisis. It is critical that both FHA and the GSEs continue to purchase these loans and do so without any additional penalties that both entities included during their now-expired pandemic flexibilities.

Chapter 3: The Impact of the COVID-19 Pandemic on Properties

Today's hot housing market features a significant imbalance between supply and demand. As noted above, the lack of inventory is especially acute in more affordable price ranges. Additionally, existing properties are often sold in ways that are difficult for homebuyers using mortgages to access. We must protect the supply of homes available for sale to homeowners purchasing with mortgages if we are going to increase homeownership for people of color rather than lose ground during the crisis.

A. Home Sales in Many Markets Are Strong

The continued strong demand in housing markets continues to drive up home prices. As of the fourth quarter of 2020, median home prices increased by more than 10 percent over the past year in 88



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percent of metro areas, and not a single metro area saw prices decline.⁶³ Home sales reflect this strong demand as well. In 2020, home sales grew almost six percent from 2019 levels, and experts estimate that in 2021, home sales will increase by up to 21.9 percent, the most significant annual sales growth since 1983.⁶⁴ This surge in home price appreciation and home sales growth raises concerns that homeownership will become less affordable and accessible.

Due to decades of discrimination and the racialized nature of housing demand in this country (see sidebar), communities of color generally have weaker housing markets. Yet, given the severe supply shortage, our country faces, even some communities of color have seen high rates of home price appreciation. In metropolitan areas with moderate or high levels of appreciation overall, homebuyers in racially diverse and lower-income neighborhoods tended to see more appreciation of their home values during the 2012-2017 recovery.⁶⁵ Critically, however, in metropolitan areas with weaker housing markets, racially diverse and lower-income neighborhoods saw less price appreciation during this period than other neighborhoods.

Race Affects the Homebuying Process From Start to Finish

Research has demonstrated that White homebuyers mainly search for homes in White communities, while Black homebuyers search in communities with a variety of racial compositions.⁶⁶ Moreover, investigations reveal that many consumers are steered to certain areas based on race. A recent investigation on Long Island by *Newsday* found that people were steered to communities based on their race or ethnicity. In their search to purchase a home, Blacks faced unequal treatment 49 percent of the time, Latinos 39 percent of the time, and Asian Americans 19 percent of the time.⁶⁷ Steering was found in 24 of 86 tests overall; this mirrors a multi-year investigation by the National Fair Housing Alliance (“NFHA”) that found similar discriminatory results.⁶⁸ Segmented demand and unfair practices reduce demand and home values in communities of color. A 2018 Brookings Institution study found that owner-occupied homes in Black neighborhoods were undervalued by \$48,000 per home on average, leading to \$156 billion in less wealth for these homeowners.⁶⁹

⁶³ “All Metro Areas Saw Home Prices Rise during Fourth Quarter of 2020,” National Association of REALTORS[®], February 11, 2021, <https://www.nar.realtor/newsroom/all-metro-areas-saw-home-prices-rise-during-fourth-quarter-of-2020>.

⁶⁴ “Bold 2021 Predictions: A Stronger Housing Market across the Board,” Zillow, December 18, 2020, <https://www.zillow.com/research/zillow-2021-housing-predictions-28516/>

⁶⁵ Dan Immergluck, Stephanie Earl, and Allison Powell, “Black Homebuying after the Crisis: Appreciation Patterns in Fifteen Large Metropolitan Areas,” *City & Community* 18, no. 3 (August 21, 2019): 983–1002, <https://doi.org/10.1111/cico.12436>.

⁶⁶ Maria Krysan, “Does Race Matter in the Search for Housing? An Exploratory Study of Search Strategies, Experiences, and Locations,” *Social Science Research* 37, no. 2 (June 2008): 581–603, <https://doi.org/10.1016/j.ssresearch.2007.06.001>.

⁶⁷ Ann Choi et al., “Long Island Divided,” *Newsday*, Nov. 17, 2019, <https://projects.newsday.com/long-island/real-estate-agents-investigation/>.

⁶⁸ Cat Cloud et al., “Fair Housing Solutions: Overcoming Real Estate Sales Discrimination,” National Fair Housing Alliance, December, 2019, <https://nationalfairhousing.org/wp-content/uploads/2019/12/Fair-Housing-Solutions-Overcoming-Real-Estate-Sales-Discrimination-2.pdf>.

⁶⁹ Andre M. Perry, Jonathan Rothwell, and David Harshbarger, “The Devaluation of Assets in Black Neighborhoods: The Case of Residential Property,” Brookings Institution, November 27, 2018, <https://www.brookings.edu/research/devaluation-of-assets-in-black-neighborhoods/>.



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National Association of REALTORS® President Charlie Oppler issued a formal apology in November 2020, acknowledging the industry's role contributing to racial segregation and inequality in America. Oppler noted that "Because of our past mistakes, the real estate industry has a special role to play in the fight for fair housing." Today, NAR advocates for policies to close the racial homeownership gap and is engaged in accountability, culture change, and training efforts to stamp out discrimination in real estate.

B. There Is a Supply Crunch, Especially in the More Affordable Value Bands

The United States is not building enough new housing to meet growing demand and replace the units lost each year due to age and deterioration.⁷⁰ For example, in 2017, the 1.25 million units of new housing built were 370,000 units short of what was needed. All told, due to underbuilding since the Great Recession, Freddie Mac's chief economist says the United States is 3.8 million housing units short of what is needed to match long-term demand.⁷¹

Another measure of housing market supply is "months' supply" of homes for sale, which measures how long it would take for the current inventory of homes on the market to sell given the current sales pace. Historically, six months of supply is considered healthy, but in recent years, months' supply available has ranged from three to four months.⁷² In January 2021, months' supply fell to 1.9 months, setting a record low for the fifth month in a row.⁷³

The supply shortage is felt most acutely in the more affordable or "starter home" segment of the market. The number of homes listed for sale at less than \$200,000 has fallen by about half over the past three years, while the number of homes for sale in other price ranges has remained relatively constant.⁷⁴

One driver of this trend is the inadequate production of new housing supply. Nationwide, the number of new residential units starting construction, or housing starts, has been dramatically depressed since the Great Recession.⁷⁵

Another driver of the supply shortage is that current homeowners are staying in their homes longer. Today, the average home seller has lived in their home for about eight years, up from an average of four to 4.5 years between 2000 and 2009.⁷⁶

⁷⁰ Sam Khater, "One of the Most Important Challenges our Industry will Face: The Significant Shortage of Starter Homes," Freddie Mac, April 2021. http://www.freddiemac.com/perspectives/sam_khater/20210415_single_family_shortage_page.

⁷¹ Ibid.

⁷² Meredith Dunn, "Inventory and Months' Supply," National Association of REALTORS®(R), January 22, 2021, <https://www.nar.realtor/blogs/economists-outlook/inventory-and-months-supply>.

⁷³ Laurie Goodman et al., "Housing Finance At A Glance: A Monthly Chartbook, February 2021," Urban Institute, February 25, 2020, <https://www.urban.org/research/publication/housing-finance-glance-monthly-chartbook-february-2021>.

⁷⁴ "National Market Outlook June 2020," Realtor.com, June 2020, <https://www.realtor.com/research/market-outlook/>.

⁷⁵ "Housing Starts: Total: New Privately Owned Housing Units Started," Federal Reserve Bank of St. Louis, accessed December 2020, <https://fred.stlouisfed.org/series/HOUST>.

⁷⁶ "U.S. Home Seller Profits Rise To 36 Percent In Second Quarter Of 2020," ATTOM Data Solutions, July 23, 2020, <https://www.attomdata.com/news/market-trends/home-sales-prices/attom-data-solutions-q2-2020-u-s-home-sales-report/>.



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Yet a third driver, perhaps much less appreciated in the national conversation, is how homes are being sold. In short, many homes are sold through processes that owner-occupants often do not use and that favor cash investors over a family with a mortgage.

C. Investor Purchases of REO Properties

As last decade's financial crisis unfolded, investors of all sizes, from local investors buying one property to large investment firms like Blackstone Group and American Homes 4 Rent, among others buying thousands at a time, purchased REO properties *en masse*. These purchases were often in cash and were often at prices far below the market value. Some investors "flipped" these properties at a profit. Other investors let their properties sit vacant in the hopes that property values would appreciate over time without any investment on their part. More often than ever before, others turned their properties into rental units, some amassing scattered site rental portfolios of tens of thousands of units.⁷⁷

These wide-scale investor purchases of REO properties resulted in previously high-homeownership neighborhoods evolving into rental-dominated communities. This change to homeownership access was often most notable in communities of color that had previously had significant homeownership rates since foreclosures were concentrated in Black and Latino neighborhoods.

Today, the problem of cash investor displacement of owner-occupants has expanded from REO sales through the entire range of ways in which homes are sold. It occurs at foreclosure auctions, which are often held online now, and it occurs in sales of non-performing loans (individual and bulk sales). Increasingly, even short sales are held on auction sites, where investors purchase them with cash rather than by a new homeowner. MLS sales also attract buyers offering all cash, who are much more likely to buy any home than potential purchasers using a mortgage.⁷⁸

REO Sales in Memphis, TN

In the Memphis, TN metro area, NFHA reviewed the sale outcomes for 231 REO properties investigated from 2013 to 2017. As illustrated in Figure 3, poorly maintained REO properties sold to investors at a much higher rate than well-maintained REO properties. Significantly higher shares of REO properties in communities of color sold to investors rather than to owner-occupants. The initial sales price also varied greatly across communities: in White communities, REO properties sold for an average of \$152,280, while REO properties in communities of color sold for an average of \$32,565.

⁷⁷ Julia Gordon, "The Dark Side of Single-Family Rental," *Shelterforce* July 2018, <https://shelterforce.org/2018/07/30/the-dark-side-of-single-family-rental/>; Christopher E. Herbert, Irene Lew, and Rocio Sanchez-Moyano, "The Role of Investors in Acquiring

Foreclosed Properties in Low- and Moderate-Income Neighborhoods: A Review of Findings from Four Case Studies," Harvard Joint Center for Housing Studies, 2013, <https://www.urban.org/sites/default/files/publication/24171/412950-The-Role-of-Investors-in-Acquiring-Foreclosed-Properties-in-Low-and-Moderate-Income-Neighborhoods-A-Review-of-Findings-from-Four-Case-Studies.PDF>

⁷⁸ According to Redfin, offering all cash nearly quadruples a buyer's chance of winning a bidding war. Dana Anderson, "All-Cash Offers Quadruple a Homebuyer's Chances of Winning a Bidding War," Redfin, March 22, 2021, <https://www.redfin.com/news/most-effective-bidding-war-strategies-2020-2021/>.

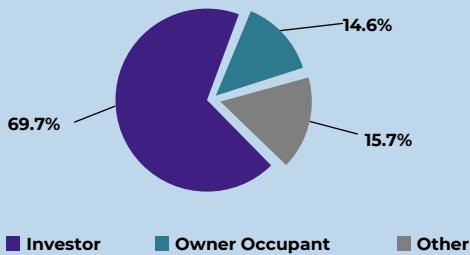


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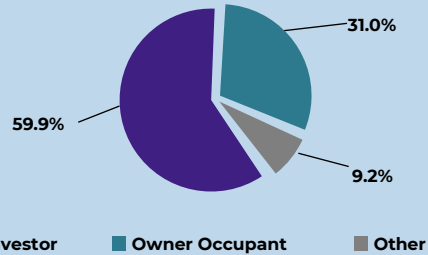
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Figure 3: Shelby County, TN Disposition Outcomes for REO Properties by Maintenance Status

Disposition Outcomes for REO Properties in Communities of Color
Shelby County, TN

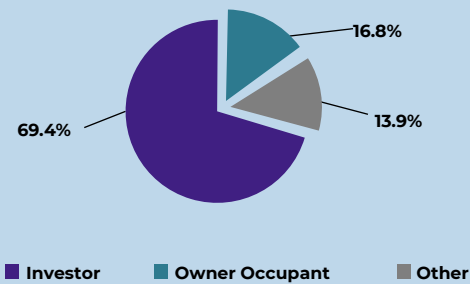


Disposition Outcomes for REO Properties in White Communities
Shelby County, TN

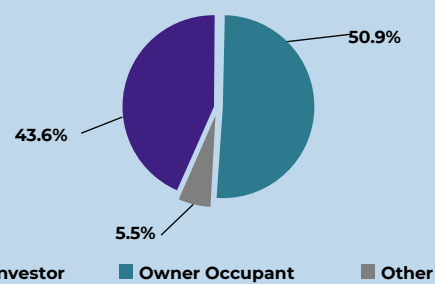


Shelby County, TN Disposition Outcomes for REO Properties by Neighborhood Demographics

Disposition Outcomes for REO Properties in Communities of Color
Shelby County, TN



Disposition Outcomes for REO Properties in White Communities
Shelby County, TN



D. Improper Maintenance of Foreclosed Homes Devalues Communities and Restricts Opportunities for Homeownership

How institutions treat REO properties that they own following foreclosure can either support and stabilize a community or cause blight and debilitate a neighborhood.

As the foreclosure crisis began to unfold, NFHA and 21 of its local member fair housing organizations conducted a comprehensive nationwide investigation into how REO assets were maintained and marketed. These investigations were undertaken in more than 60 cities, beginning in 2009 and spanning nine years. NFHA has published three reports describing its findings.⁷⁹

NFHA's REO investigations uncovered widespread discrimination in the maintenance and marketing of REO properties in communities of color.⁸⁰ Overall, REO properties in higher-income, White

⁷⁹ See "Foreclosure Crisis and Recovery," National Fair Housing Alliance, <https://nationalfairhousing.org/reo/>.

⁸⁰ From 2016 to 2018, NFHA and its fair housing partners filed three separate federal lawsuits against Fannie Mae; Bank of America and Safeguard Properties Management LLC; and, Deutsche Bank, Ocwen Financial Corporation, and Altisource



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neighborhoods were well maintained with minimal maintenance and marketing deficiencies. For example, properties in predominantly White areas were much more likely to have professional “for sale” signs prominently displayed in the yard or windows, have trimmed grass and shrubs, and have secured doors and windows. However, REO properties in communities of color were much more likely to have many more deficiencies, including significant amounts of trash and debris, overgrown grass and invasive plants, and unsecured or broken doors and windows, accumulated mail, and other maintenance failures.

The inconsistent and substandard fashion in which REOs in communities of color were maintained negatively affected the surrounding neighborhoods. Academic research demonstrates that foreclosures lower the values of neighboring homeowners’ homes⁸¹; erode property tax revenue and increase costs for municipal governments associated with having to intervene in the maintenance of these bank-owned homes⁸²; and, damage neighborhood health and safety.⁸³ Given what we know about servicer REO maintenance practices, these impacts were most likely felt the hardest in communities of color.

E. Recommendations

Two strategies to prevent the housing supply shortage from becoming worse are:

- 1. Prioritize the sale of previously owner-occupied homes to new owner-occupants rather than convert them to rentals.**
- 2. Keep homes properly maintained, so they continue to be habitable and to prevent neighborhood blight.**

In order to do this, we need to:

- a. Prioritize homeownership and neighborhood stabilization in distressed and REO sales;*
- b. Prevent zombie foreclosures and aggressively address vacancy; and,*
- c. Properly maintain REO properties in all neighborhoods.*

a. Prioritize homeownership and neighborhood stabilization in distressed and REO sales.

Distressed sales

Distressed sales consist of pre-foreclosure sales, including short sales, foreclosure sales, post-foreclosure third-party sales, and REO sales. When the GSEs, FHA, and other investors engage in

Portfolio Solutions for their discriminatory maintenance and marketing of REO properties in communities of color throughout the country. As of February 2021, all three lawsuits are pending in federal court. For more information regarding NFHA’s federal lawsuits, see <https://nationalfairhousing.org/case-settlement-information/>.

⁸¹ John Y. Campbell, Stefano Giglio, and Parag Pathak, “Forced Sales and House Prices,” *American Economic Review* 101 (5) (2011).

⁸² William C. Apgar, Mark Duda, and Rochelle Nawrocki Gorey, “The Municipal Cost of Foreclosures: A Chicago Case Study” Homeownership Preservation Foundation, 2005, available at <https://www.issueab.org/resources/1772/1772.pdf>

⁸³ G. Thomas Kingsley, Robin Smith, and David Price, “The Impacts of Foreclosures on Families and Communities,” Urban Institute, 2009, <https://www.urban.org/sites/default/files/publication/30426/411909-The-Impacts-of-Foreclosures-on-Families-and-Communities.PDF>



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distressed sales, we recommend favoring property sales to owner-occupants and nonprofit organizations. Removing incentives for selling these homes to investors and providing a path for owner-occupants or mission-oriented entities to purchase foreclosed homes will help build wealth for families, stabilize neighborhoods, and create affordable housing options.

To achieve these goals, we first recommend that distressed properties be sold through “First Look” programs, which give specific buyers an exclusive right to purchase homes before they are listed on the open market. These programs increase the likelihood that owner-occupants or mission-focused buyers will acquire the properties instead of other investors. More robust still are programs that trigger additional First Look periods if a property’s sales price is reduced. Concurrently, policymakers should consider ways to strengthen the capacity of nonprofits to acquire and rehabilitate single-family properties, including by increasing capital availability, technical assistance, and public subsidy for this work.

NCST’s REOMatch™ & REOTrack™,

The National Community Stabilization Trust (“NCST”) runs a unique transaction platform called REOMatch™ to facilitate sales of single-family REO properties to nonprofit and mission-aligned developers, as well as to land banks and municipalities. Most of NCST’s buyers rehabilitate these REO properties and return them to productive use. Primarily, they rehabilitate properties for resale to owner-occupants, but some use them as affordable rentals or hold them in a land bank for future use. By facilitating property sales to a network of vetted, community-based, nonprofit, and mission-focused for-profit organizations, NCST’s program, which has put more than 27,000 properties back to productive use over the last 12 years, strengthens neighborhoods, prevents blight, and provides affordable homeownership opportunities. NCST also operates a partner platform called REOTrack™, where buyers report on the nature and extent of the rehabilitation and disposition of the property. Forthcoming research finds that compared to other buyers of distressed properties, NCST buyers are more likely to renovate properties lower-income communities of color and sell these properties to owner-occupants.⁸⁴

FHA’s REO sales process provides a number of homeownership and nonprofit acquisition opportunities, including a 15-day First Look period for homeowners, nonprofits, and government agencies, as well as the Good Neighbor Next Door program that gives teachers, firefighters, police officers, and nonprofits access to properties at a significant discount in revitalization areas. These are commendable programs, and HUD should examine each of them to see if they can be improved or further expanded.

There are several additional steps lenders and GSEs should take to sell properties to owner-occupants and nonprofits:

- Avoid the bulk sale of REO properties;

⁸⁴ Andrew Jakobovics and David Sanchez, Forthcoming, “Does a Non-Profit “First Look” Program Promote Neighborhood Stabilization? Examining Outcomes for REO Sales in Florida,” Center for Community Progress, Federal Reserve Bank of Atlanta, and Federal Reserve Bank of Cleveland, “Ten Years Tackling Vacancy and Abandonment: A Retrospective Examination of Strategies and Impacts.”



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- Establish close partnerships with professional real estate organizations that facilitate sales to owner-occupants;
- Market REO properties broadly, and do not list REO properties solely on auction websites;
- Repair a greater share of REO properties before marketing so that they are good candidates for purchase by owner-occupants;
- To the extent possible, allow for property inspections and inspection, appraisal, and financing contingences; and,
- Ensure that auction websites allow owner-occupant buyers who require financing to compete equally with “cash only” offers. To help facilitate this, the GSEs and FHA should examine this issue and eliminate barriers to using their loan products to purchase properties that require repairs.

Improve Bulk Note sales

During the last foreclosure crisis, Fannie Mae, Freddie Mac, and FHA established programs to auction off non-performing loans (“NPLs”). The primary goal of these programs was to get these assets off the books of the agencies, shoring up their balance sheets while avoiding the costs associated with going through the foreclosure process and then managing the foreclosed properties. A secondary goal was to enable better loss mitigation for homeowners still in their homes, either due to greater flexibility or because no one expected the original servicers to do the loss mitigation required.

By the end of 2019, the GSEs had sold 126,757 NPLs⁸⁵ while FHA sold 108,709 single-family loans between 2012 and 2016.⁸⁶ Through a similar program, HUD also sold about 6,000 reverse (HECM) mortgages since 2016.⁸⁷

One of the notable aspects of FHA’s note sales program was the creation of smaller pools called Neighborhood Stabilization Outcome (NSO) pools. These requirements were intended to elevate loss mitigation strategies that would preserve homeownership to the greatest extent possible and result in less blight in neighborhoods. While a relatively small percentage of overall FHA NPL sales took place through these NSO pools, they delivered significantly better performance by some key measures, particularly those sales that involved mission-driven nonprofit organizations in some form.

The GSEs also tried to improve their note sales, placing specific requirements on how all NPL buyers must conduct loss mitigation, property maintenance, and REO sales.

We recommend that any future sales of federally-backed non-performing loans—either forward or reverse mortgages—establish homeownership preservation and neighborhood stabilization as priorities equal to any financial benefits that such sales may provide. To accomplish this, we

⁸⁵ “Enterprise Non-Performing Loan Sales Report,” Federal Housing Finance Agency, December 2019, https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/Dec-2019_NPL-Sales-Report.pdf.

⁸⁶ “Report to the Commissioner on Post Sale Reporting; Single Family Loan Sales of Distressed Asset Stabilization Program Loans,” U.S Department of Housing and Urban Development Federal Housing Administration, February 2020, <https://www.hud.gov/sites/dfiles/Housing/documents/CReport.pdf>. Does not include 2,055 2010-2012 SFLS sales.

⁸⁷ “Report to the Commissioner on Post Sale Reporting: HUD-Held Vacant Loan Sales for Home Equity Conversion Mortgages,” September 2020 Report, https://www.hud.gov/sites/dfiles/Housing/images/HVLSCReport_September2020_v2_Clean.pdf.



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recommend the following provisions, which encompass some of the best practices of both FHA and the GSEs:

- Bulk note sales should only be done in emergencies, not as a regular course of business;
- Mission-driven organizations working to assist homeowners and neighborhoods should be able to compete successfully in NPL sales. While programs prioritizing women and minority business owners are also valuable, they are not equivalent to or a substitute for entities that work in affordable housing or community development;
- Before auctioning NPLs, which drives up prices often to a point where certain types of neighborhood-positive outcomes are impossible, holders of federally-backed mortgages should first try to arrange direct sales to municipalities and qualified nonprofits;
- Establish systems to ensure that servicers do not use notes sales as a mechanism to avoid loss mitigation requirements that would otherwise apply to any loans or to avoid requirements related to distressed properties;
- Provide advance written notice to borrowers that their loans are about to be included in a note sale;
- Require investors who purchase NPLs to offer homeowners a range of loss mitigation options as good as or better than the options available prior to the sale;
- For any vacant properties identified in NPL pools, or any properties that become vacant because there was no feasible home retention option possible for the homeowner, establish a First Look program mandating a period during which the property will only be available for purchase by a prospective owner-occupant or a nonprofit whose mission includes community stabilization; and,
- Require purchasers to collect and report information on the demographics (race, sex, national origin) of the borrower, geographic location (preferably census tract) of the property, and resolution of the loan, which is critical to facilitate monitoring and evaluation of the program and to ensure fair and non-discriminatory treatment for all borrowers whose loans are included in any NPL sales. The data should be reported to the appropriate federal agencies, and investor-specific, loan-level data should be made available to the public.

CWCOT

In recent years, FHA has significantly expanded its Claim Without Conveyance of Title (“CWCOT”) Program. The CWCOT program allows a servicer to file an FHA insurance claim if it can sell the property to a third party for a HUD-approved price at the foreclosure sale or during a 60-to-90-day period after the foreclosure sale (“second chance” sales). This program is an alternative to the typical process whereby a property would be conveyed to HUD and become HUD REO.

Servicers prefer the CWCOT system because the FHA REO conveyance process is slow, which causes the property to remain vacant longer and potentially deteriorate. It is also expensive for servicers, who face significant penalties if they miss HUD-prescribed deadlines and for HUD itself, which generally recovers less money when properties are conveyed to them than from other options.



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Because properties that flow through CWCOT never enter HUD's REO portfolio after foreclosure, these properties are not subject to the homeownership and nonprofit acquisition opportunities provided through HUD's REO program discussed earlier in this paper.

A growing share of FHA foreclosures are sold through CWCOT. In the past four years, the percentage of FHA foreclosures sold through CWCOT doubled from 29 percent to 58 percent.⁸⁸ The share of properties sold this way should continue to increase due to CWCOT program simplifications and flexibilities introduced by FHA in 2020, including refining and generally increasing the discounts applied to these properties' sales prices.

Additionally, the preponderance of CWCOT sales occurs through auction websites rather than on the Multiple Listing Service, which is how most families shop for homes. While theoretically, those auction websites are open to the public and real estate agents, many pose significant obstacles to participation by homeowners, such as listings that specify cash-only offers or the need for a deposit in an account to be an active buyer. Auctions are generally designed to attract as many bidders as possible and drive up the sales price for a home, especially in today's context where there is a shortage of affordable homes. As currently structured, CWCOT overwhelmingly facilitates sales to investors rather than homeowners.

HUD should change the CWCOT rules to prioritize selling foreclosed properties to owner-occupants whenever possible. To do so, HUD should explore requiring that CWCOT sales provide for a First Look sales period for nonprofits and owner-occupants. HUD should also explore requiring that CWCOT sales be conducted on platforms that are fully accessible by typical homebuyers and nonprofits, including by allowing the use of conventional and FHA financing. Finally, HUD should explore whether to provide additional discounts on sales to owner-occupants and nonprofits who rehabilitate properties for owner-occupants.

Pre-foreclosure sales

Because we expect pre-foreclosure sales, including short sales, to become more common in the coming years, it will be important to monitor whether investors disproportionately purchase these homes. We recommend exploring reforms to pre-foreclosure sale policies to prioritize sales to owner-occupants and investors if this occurs.

b. Prevent zombie foreclosures and aggressively address vacancy problems.

"Zombie" or abandoned foreclosures occur when a homeowner has vacated the property after learning that the servicer intends to or has initiated the foreclosure process, but the servicer does not complete either the foreclosure process or the foreclosure sale. Fearing eviction, many homeowners without legal representation leave the property in advance of a legal requirement to vacate.

In these circumstances, the absent homeowner remains the owner of record and is responsible for maintaining the property. In addition, the property remains vacant, typically to the detriment of the property itself, the immediate neighbors, and the surrounding community. Depending upon the

⁸⁸ "Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund: Fiscal Year 2020," U.S. Department of Housing and Urban Development, November 13, 2020, <https://www.hud.gov/sites/dfiles/Housing/documents/2020FHAAnnualReportMMIFund.pdf>.



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actions of the mortgage servicer, property taxes and condominium and homeowner association dues might not be paid, or the property may fall into disrepair and may not be fully secured. Abandoned properties quickly become a blight on the neighborhood, depress neighborhood property values, and are susceptible to vandalism, squatters, and crime.

Often a servicer's decision to abandon foreclosure on a property is motivated by financial considerations. When a property is of very low value, an investor may conclude the cost of foreclosure would outweigh what it expects to recover on the property. In these circumstances, servicers "walk away" from the property. In doing so, they give up collection efforts on the loan, may release any liens on the property, and give up any responsibility to secure or maintain the property. Walking away is especially damaging to communities if a property is vacant or abandoned. At the direction of FHFA, Fannie Mae and Freddie Mac no longer release liens and abandon foreclosure efforts on properties that would blight neighborhoods, including those that are vacant or abandoned.⁸⁹ Other investors should follow this model.

While zombie foreclosures are a significant problem, they are not the primary source of vacant or abandoned properties. The overwhelming majority of vacant properties—about three quarters as of 2017—are owned by investors rather than owner-occupants.⁹⁰ Especially in weaker housing markets, many investors have simply left the properties vacant, where they continue to blight neighborhoods and depress local housing values.

Local and state governments use various tools to mitigate the negative impact that vacant properties have on communities. Returning these properties to productive use should remain a high priority for state and local governments. Particularly promising are tools that facilitate the transfer of abandoned properties to new owners. One model is Baltimore's receivership process, whereby the city can quickly clear liens and transfer ownership to a private party with a demonstrated ability to rehabilitate the property immediately.⁹¹

c. Properly maintain REO properties in all neighborhoods.

To avoid a repeat of the adverse outcomes witnessed during the Great Recession and to ensure that homes are properly maintained, it is essential that the following be addressed:

- Lenders and GSEs should implement strong quality control measures and compliance penalties to ensure that the property preservation companies they hire conduct exterior and interior REO maintenance correctly and in a non-discriminatory manner. Particular attention should be directed to neighborhoods most vulnerable to poor maintenance by property preservation

⁸⁹ For additional details, see Freddie Mac Servicing Bulletin 2018-2 at <https://guide.freddie.com/app/guide/bulletin/2018-2> and Fannie Mae Servicing Guide Announcement SVC-2018-01 at <https://singlefamily.fanniemae.com/media/4971/display>.

⁹⁰ Robert Finn and Julia Gordon, "Fast Track Foreclosure Laws: Not a Silver Bullet for Fighting Blight," National Community Stabilization Trust, August 2018, <http://www.stabilizationtrust.org/wp-content/uploads/2018/08/NCST-Fast-Track-Foreclosure-Report-Final-smaller-8.14.2018.pdf>.

⁹¹ James J. Kelly Jr., "Refreshing the Heart of the City: Vacant Building Receivership As a Tool for Neighborhood Revitalization and Community Empowerment," *Journal of Affordable Housing & Community Development Law* 13, no. 2 (2004): 210-38, <http://www.jstor.org/stable/25782687>.



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companies, including neighborhoods deemed “investor” neighborhoods; Black, Latino, and Asian communities; and low- or moderate-income communities.

- Lenders and GSEs should carefully select and train their REO property brokers and vendors. All parties should be trained on the Fair Housing Act, should not be the subject of any pending complaints of discrimination, and should have successfully resolved any prior complaints of discrimination. Lenders and GSEs should prioritize local agents, property preservation companies, and real estate professionals who can closely manage and oversee the treatment of each REO property to which they are assigned.
- Lenders and GSEs should maintain and market REO properties equally in all neighborhoods, in accordance with fair housing laws and local code enforcement regulations.
- Lenders and GSEs should maintain a public database of all REO listings and include the name and contact information of preservation management companies and/or brokers and ensure that vendors and brokers are posting accurate and legible contact information at each property.
- Local governments should implement Vacant Property Registries, requiring banks and other owners to register their vacant properties and provide up-to-date contact information for parties responsible for any maintenance or other issues that may arise on the property. Local jurisdictions with such registries should step up enforcement of their requirements.

Chapter 4: Conclusion

The COVID-19 pandemic threatens to push hundreds of thousands of homeowners into foreclosure, damaging their ability to sustain or re-enter homeownership after the crisis. Most at risk are borrowers of color and lower-income borrowers. This comes at a time when mortgage lenders are restricting access to credit and when our country faces a housing shortage, especially of more affordable homes. While home sales are very strong, the housing supply shortage raises concerns about worsening affordability. A new generation of increasingly diverse homebuyers appears ready to assume homeownership. However, the housing market must meet these buyers with homes they can afford and must make affordable and sustainable credit accessible to them.

As we respond to this pandemic, we must chart a different course than we did in the aftermath of the Great Recession. Rather than allowing unnecessary foreclosures and home loss to occur, we must help households sustain homeownership and maintain strong credit profiles. Rather than tightening access to credit, we must ensure that households can obtain sustainable and affordable loans. Rather than letting foreclosed properties blight communities, we must maintain these properties for homeownership. Finally, rather than disproportionately selling properties or notes to investors, many of whom will turn them into rental properties, we must prioritize the sale of these properties to owner-occupants or nonprofits that rehabilitate them for homeownership. These steps will strengthen our communities and allow a new generation to build wealth through homeownership.

